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OVERSIGHT OF CABLE TV

HEARINGS

BEFORE THE

SUBCOMMITTEE ON COMMUNICATIONS

OF THE

COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION
UNITED STATES SENATE

ONE HUNDRED FIRST CONGRESS

FIRST SESSION

ON

THE OVERSIGHT OF THE 1984 CABLE TELECOMMUNICATIONS ACT

NOVEMBER 16 AND 17, 1989

Printed for the use of the Committee on Commerce, Science, and Transportation

U.S. GOVERNMENT PRINTING OFFICE
25-079 O WASHINGTON : 1990

S261-26

For sale by the Superintendent of Documents, Congressional Sales Office
U.S. Government Printing Office, Washington, DC 20402

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OVERSIGHT OF THE 1984 CABLE TELECOMMUNICATIONS ACT

THURSDAY, NOVEMBER 16, 1989

U.S. SENATE,
SUBCOMMITTEE ON COMMUNICATIONS,
COMMITTEE ON COMMERCE,
SCIENCE, AND TRANSPORTATION,
Washington, DC.

The Subcommittee met, pursuant to notice, at 9:07 a.m., in room SR-253, Russell Senate Office Building, Hon. Daniel K. Inouye (chairman of the subcommittee) presiding.

Staff members assigned to these hearings: Tom Cohen and Toni Cook, staff counsels; and Gina Keeney, minority staff counsel.

OPENING STATEMENT BY SENATOR INOUYE

Senator INOUYE. Good morning.

At the beginning of the 101st Congress, it was apparent that many Americans were troubled about the market power of the cable television industry and were hopeful that the Subcommittee would make an examination of this issue a priority.

The Communications Subcommittee, accordingly, decided to hold a series of hearings to determine the nature of the problems that exist in the marketplace and to decide whether legislation was necessary.

The first set of hearings on media ownership was held this past June, and Members of the Subcommittee participated extensively in those hearings, and we gained important insights into the nature and current trends of the media industry, including cable television.

The purpose of the hearings this morning and tomorrow is to examine in greater depth the particular provisions of the 1984 Cable Telecommunications Act.

The 1984 Act establishes a national policy that clarifies the current system of local, State, and Federal regulation of cable TV.

Until the 1984 Act, there was no Federal policy for cable television. The Federal Communications Commission had only indirect authority to oversee the cable industry, which it obtained by virtue of its obligation to insure that broadcasters serve the public interest.

About a dozen States had laws in effect controlling certain cable activities, and in those States where no law existed, the cities and other local government entities exercised control because cable systems had to pass through public rights of way.

As a result, the cable industry was subjected to a crazy-quilt of regulation, often to its detriment and to that of the subscriber.

The 1984 Act changed the cable landscape significantly.

It defined more precisely the roles of each governmental entity. The State or local authorities continued to control the franchising process, but under new constraints.

The Federal Government controlled basic rate deregulation and technical standards.

We now have five years of experience with the 1984 Act. In that time, we have seen the cable industry grow tremendously, and we have seen great changes in the video media.

It is time for this Subcommittee to review where we stand. What are the effects of the Cable Act?

After these two hearings, I will discuss with the Members of the Subcommittee whether any of the effects are so inimical to the public interest that legislation may be necessary.

Today, we will hear from parties most deeply involved in the 1984 Act: the cable industry, the cities, and the consumers.

Testifying on the first panel for the cable industry will be Mr. James Mooney, President of the National Cable Television Association; Mr. John Malone, President of TCI; and Mr. James Robbins, President of Cox Cable Communications.

The second panel will consist of five witnesses from various cities or franchising authorities. They are Sharpe James, the Mayor of Newark, New Jersey, representing the National League of Cities and the United States Conference of Mayors; Charles Edward Patterson, the Mayor of Henderson, Tennessee; Mr. Dennis Collins, the Mayor of Bayonne, New Jersey; Mr. Robert Alm, the Director of Commerce and Consumer Affairs for the State of Hawaii; and Mr. Saul Ramirez, the Mayor Pro-Tem of Laredo, Texas.

The final panel will consist of Mr. Gene Kimmelman, Legislative Director, Consumer Federation of America; and Ms. Sharon Ingraham, Chairperson, National Federation of Local Cable Programmers.

Do my colleagues have any statements at this time?

Senator Packwood. No statement, Mr. Chairman.

Senator Inouye. Are there any statements on this side?

OPENING STATEMENT BY SENATOR FORD

Senator Ford. Mr. Chairman, I want to compliment you first for your efforts in this direction. I am pleased that you've called the hearing this morning to review our work in 1984, which, basically, deregulated the cable industry.

I have had some problems with the philosophy of the big cable operators. I believe that their view of government relations is the "scorched earth theory," in that they beat back every single legislative initiative or suggestion.

No one would suggest that there have not been problems with some of the provisions of the Cable Regulation Act. If we had been able to remedy some of those problems, then I do not believe that it would be necessary for us to be here today.

There are many fine cable operators in Kentucky. In fact, most are providing excellent service.

Unfortunately, they are going to have to live with legislation that may go as far as rate reregulation because of problems in which they are not involved.

I am sad that we have come to the time that we will completely change all the rules due to the actions of a few.

I have joined with the Ranking Member, Senator Danforth, in his effort to find answers to the problem of the cable industry.

I think it is significant, Mr. Chairman, that his bill is bipartisan and has 15 co-sponsors, eight of those from this Committee.

Cable issues can no longer be ignored. It is simply a question of how we fix the problems.

I look forward to the testimony in that I do have an open mind on some of the issues that will be discussed during the next two days.

Mr. Chairman, I would be remiss, and since I serve as Chairman of the Rules Committee, I cannot let this opportunity pass without saying something about the coverage of C-Span on cable systems.

I was involved in the legislation that brought about televised sessions of the Senate. The taxpayers spent a great deal of money to build the system and continue coverage.

Out of 9,000 cable systems in the United States, 3,400 provide C-Span I, which is House proceedings, and only 667 have C-Span II, which is the Senate.

Today, most cable systems are 35 channels, and there seems to be plenty of capacity for shop-at-home networks and mud wrestling—but limited coverage of democracy at work.

I think the cable industry could do a better job in providing House and Senate coverage to the citizens on their systems.

I thank you, Mr. Chairman.

Senator INOUYE. I thank you, sir.

Mr. Gore.

Senator GORE. I want to congratulate Senator Packwood for his forbearance in not making any of several comments he could have made comparing mud wrestling to the proceedings on the floor of the United States Senate.

Senator FORD. He's been very restrained this morning, and so have we.

OPENING STATEMENT BY SENATOR GORE

Senator GORE. Mr. Chairman, I want to associate myself with the remarks made by Senator Ford, and I want again to thank you, Mr. Chairman, for your leadership in examining the continuing problems facing consumers of cable television programming—cable, satellite dish, and wireless cable customers.

As I was preparing for this hearing, I reread statements that I made earlier this year, in 1988, in 1987, in 1986, and in 1985, all of them dealing with problems in the cable marketplace, one, two, three, and four years ago.

What stood out was that the case that I'll try to make today during the hearing is almost identical to the case that I and many others have been making for the past four years.

In other words, the problems which we started talking about back then haven't been solved, and the industry is still severely distorting the marketplace. Nothing has changed, and, in fact, from the consumer's standpoint, it has gotten much worse.

We now have empirical evidence citing cable rate increases since the 1984 Act which are vastly in excess of inflation. Even if you accept the GAO report of 24 to 29 percent national average increases over the past three years, that would be bad enough. But, of course, that was a sort of voluntary survey and an inaccurate survey.

But we will hear today and tomorrow of increases that are much, much more alarming—not only from the infamous Multivision System in West Tennessee, and we'll hear about that later in the testimony today.

But if you look in my home State, outside of the infamous Multivision case, the City of Memphis, in the last three years, from 1986 to 1989, had rate increases of 71 percent.

In Crossville, the rate increases have been 99 percent.

In Nashville, the rate increases have been 113 percent.

In Chattanooga, they were 115 percent.

In Murfreesboro, they were 117 percent.

In Knoxville, they were 116 percent.

Well, what's going on, Mr. Chairman?

Some place just say well, that's just the marketplace at work. If they want to raise their rates 117 percent, that's just market economics.

Well, it's a monopoly. And the Federal Government has come in and told the local governments, which grant the monopoly franchise: hands off; let them fleece the consumers as much as they possibly can; let them get their hands right in their pockets and you keep away; let them go to it and get the money as much as they can.

Well, the degree to which this industry has become vertically and horizontally integrated has now reached staggering proportions.

The huge MSOs get bigger and bigger, more and more powerful, and exercise even more anticompetitive muscle against their competitors.

TCI, for one—and we'll hear from its CEO today—is obviously hell-bent toward total domination of the market as it buys up not only more and more cable systems, but more and more major programming services, and even movie studios.

Earlier this week, in another Senate Committee there was considerable concern about the Super Bowl possibly moving to pay-per-view cable in the near future.

I think that they are focusing on the wrong danger. I think a real concern might be whether or not TCI will own the NFL outright.

Ironically, the cable MSOs vigorously oppose any competition from the only entity able to directly challenge their natural monopoly, and that is the telephone companies.

They cite the ability of the TeleCos to monopolize the delivery system.

Well, if there were ever a case of the pot calling the kettle black, this is it.

Three years after we first raised the issue of unfair program marketing practices for home satellite dish owners, there are still no non-cable distributors with competitive contracts. Not a single one.

In fact, the only non-cable distributor even offered programming rights, the National Rural Telecommunications Cooperative, has had its marketing hands hopelessly tied by unfair wholesale prices and restrictive access to consumers, and 400 percent higher rates than what they offer the cable industry distributors. And the much vaunted Showtime satellite dish wholesale rates are 83 percent higher to non-cable distributors than through cable companies.

Of course, Showtime is now being purchased by TCI also.

If distortions in the marketing of programming were not enough to cause concern, we now learn that home satellite dish owners are being forced to buy expensive, unwanted, unneeded equipment to even be able to purchase programming.

Three years ago, these 2 million mostly rural families were told that they had to spend $400 each for a decoder to be able to buy programming.

Fine, they said. We're willing to pay for what we watch. But now we find that there are no stand-alone decoders available. They are not selling them at all. And, if you can find one, it costs as much as $100 more than it did two years ago, despite the manufacturer's promise that the price would come down with volume sales. It has gone up instead.

So, once again, they want to stick rural consumers with the bill.

So, Mr. Chairman, it is time to act.

We now have six Senate bills addressing these problems. I've introduced two of them, the Cable Competition Act and the Satellite Television Fair Marketing Act, with 20 co-sponsors on one or both bills.

The point of all of the six bills before us is to give cable consumers and satellite dish owners some modest relief from skyrocketing rates and pervasive anticompetitive practices.

So, Mr. Chairman, this is an ambitious set of hearings. You have been very gracious to accommodate the concerns of so many witnesses in setting these panels. In particular, I'm looking forward to hearing Mayor Eddy Patterson of Henderson, Tennessee. He has a story that ought to put to rest any skepticism about the extremes to which some in this industry have been prepared to go in order to soak their customers.

I believe that these hearings will build a record that will argue undeniably for legislative action in this Congress.

So, thank you again, Mr. Chairman.

I look forward to moving expeditiously toward a legislative remedy for the problems we will hear about in these two days of hearings.

Senator INOUYE. I thank you very much.

Senator Hollings, do you wish to make an opening statement?

OPENING STATEMENT BY THE CHAIRMAN

The CHAIRMAN. I am pleased that we are here today to review the 1984 Cable Telecommunications Act. Cable television has been in existence for many decades, but its explosive growth did not really begin until a short time ago. The Cable Act of 1984 is one of the key reasons for this great expansion of cable television service. The Cable Telecommunications Act of 1984 brought about major changes in both federal, state and local oversight of the cable television industry. It established general franchise requirements. It provided for the deregulation of basic rates. It set aside channels for public and commercial access. It structured a franchise renewal process. It limited franchise fees. It also constructed a scheme for access to unscrambled cable programming by home satellite dish owners.

The cable industry is now well established. Over 55 percent of American homes take cable service and many more have access to this service. At the same time, there have been tremendous changes in other video distribution technologies and in the overall marketplace. These factors combined with five years of experience with the Cable Act makes this an appropriate time for this Subcommittee to review the state of the cable industry and the law.

The Committee is looking to the witnesses who will appear during these hearings to help us with our review. I know that many Senators have already heard from constituents on some of these issues, and I know Senators have tried to address these concerns in numerous bills reregulating the cable industry. I look forward to the testimony we will hear during these two days.

Senator INOUYE. Thank you. Senator Pressler would you like to make a statement?

OPENING STATEMENT BY SENATOR PRESSLER

Senator PRESSLER. Mr. Chairman, thank you for calling this set of hearings on cable television competition and regulation. This is an issue of great consumer interest that shows no immediate sign of going away by itself. Congress must do something to improve the situation.

The bill introduced yesterday by Senator Danforth, the Cable Television Consumer Protection Act, is a good comprehensive approach to the problems encountered by consumers as a result of the monopoly system in place today. I am proud to be a cosponsor of that legislation and several other pieces of legislation that aim at increasing effective competition and ensuring fair rates.

From October, 1986, to October, 1988, basic cable rates have increased 29 percent nationally. This increase is unwarranted and was made possible because of the lack of both competition and regulation. One or the other must be present or there is nothing to hold rates down. We created an unregulated monopoly and this is the result.

I am particularly pleased that Senator Danforth's legislation includes the essential elements of S. 168, a bill I introduced in January of this year. My legislation, which has been incorporated into this new bill, bars cable television programmers from discriminating among cable operators, or other multichannel video programming distributors, in price, terms, conditions, or availability of programming.

Satellite television distributors, wireless cable operators, and small, independent cable operators all have had to compete against the large multi-system operators (MSOs) for cable television programming. But they have not been able to compete on a level playing field. The MSOs and the programmers are so corporately entertwined that "outsiders" in the business have found themselves paying much more for the same programming. In some cases they have found that they could not get the programming they wanted at any price.

South Dakotans are concerned about rising cable rates. That was one of the most common complaints I heard as I traveled through the state this summer. And when rates in some South Dakota communities have increased as much as 100 percent over a two year period, those complaints appear to be justified.

Rural South Dakotans have an additional and more fundamental problem—availability of programming. In the smallest towns and on the farms and ranches in my state, people cannot get traditional cable television. They must rely on backyard satellite dishes or wireless cable. Consumers using these technologies must also be assured of quality programming at reasonable rates.

Mr. Chairman, thank you again for scheduling these hearings. I look forward to this morning's testimony.

Senator INOUYE. Thank you. Do you wish to make a statement, Senator Gorton?

OPENING STATEMENT BY SENATOR GORTON

Senator GORTON. I am pleased that the committee has seen fit to schedule two days of oversight hearings on the Cable Act of 1984.

Few of us who supported the Cable Act of 1984 could have envisioned the tremendous growth that has taken place in the cable industry in the last five years. Fifty-five percent of American households now subscribe to cable T.V. Americans enjoy new programming that would have never been available without the success of the cable industry. Yet in virtually every community, the cable company operates without effective competition.

According to the Association of Independent Television Stations, of the more than 9,000 cable systems in this country, only 36 have competition from other cable systems. Other technologies would like to offer the consumer a choice and free the consumer from the monolithic grapples of the cable industry. I'm looking forward to hearing from representatives of those industries today and tomorrow.

Yesterday, I was pleased to join with the Ranking Republican of this committee, Senator Danforth, in cosponsoring the Cable Television Consumer Protection Act. I was particularly pleased to see that we were joined by the sponsors of the dozen or so other cable bills that had been introduced earlier this year. While each of the bills takes a slightly different tack, the central message remains the same—consumers are demanding an end to an unregulated monopoly and Congress is listening and ready to respond.

Senator INOUYE. Thank you. Senator Burns?

OPENING STATEMENT BY SENTAOR BURNS

Senator **Burns**. Thank you Mr. Chairman. I commend you on the scheduling of these hearings on oversight of the 1984 Cable Communications Policy Act.

In 1984, the Congress deregulated the cable television industry. At that time, Congress accepted the argument that cable companies would be operating in a genuninely competitive environment, with consumers being able to choose from among several multichannel providers of news, information, entertainment, sports and more.

Unfortunately, that competitive environment has not fully developed. Competing cabel systems remain the exception rather than the rule and those in rural areas who could afford backyard dishes have had difficulty in receiving programming at prices equal to those paid by cable subscribers.

Let us not forget, however, the benefits brought about by deregulation. The cable industry has made substantial investments in programming, plant and equipment—investments that have directly benefitted consumers.

As an advocate of competition and deregulation in competitive environments, I must strongly emphasize that I believe that any solution to the so-called "cable problem" must include opening up the video delivery industry to full and fair competition.

As a result, Mr. Chairman, over these two days of hearings, I believe that a majority of the time should be spent examining:

First—the lack of competition in what the American consumer views as cable television service—the provision of a full complement of channels of news, information, entertainment, sports and other programming services (As I noted earlier, the anticipation that such competition would exist was an important underlying principal of the 1984 Cable Act.);

Second—the vast number of mostly rural communities in this country—like many in my home state of Montana—which remain unserved by cable or underserved by delivery systems which have failed to or been unable to deliver a full complement of cable services;

Third—the deployment of fiber optic cable and the increased consumer services which fiber can provide; and

Fourth—telephone company entry into the provision of video programming services and whether telephone company entry might solve the problems that have arisen since the passage of the 1984 Cable Act.

Again, thank you Mr. Chairman for calling these hearings to address vital communications policy issues, which are of importance to all Americans.

Senator **Inouye**. I have statements from Senators Bentsen and Breaux that I will include in the record at this point.

Opening Statement by Senator Bentsen

Mr. Chairman, members of the Subcommittee, ladies and gentlemen, I am pleased that these cable oversight hearings are being held. For quite some time now, we have heard rumblings about the problems in the cable industry. Many of my constituents, one of which you will hear from today, the City of Laredo (and I welcome them to the subcommittee), have written, called, and visted my office to state their views about "what's wrong with cable." At first it would be fair to say that many of the complaints I heard were simply grumblings from people resistant to the changes induced by the Cable Telecommunications Act of 1984. But the nature of those complaints began to change sharply within the last two years. In many communities, rates didn't just creep up, they soared. According to a survey recently provided to me by the U.S. Telephone Association, cable rates in Texas have increased an average of 80% in three years. In Dallas, for example, the basic service rate in 1986 was $2.95. It is now about $14.95. That is a 407 percent increase! The City of Laredo has seen its basic rates increase over 150% within three years. Basic services in Wichita Falls went from $6.00 per month in 1986 to $18.69 in 1989. That's a 212% increase. But it wasn't just rate hikes that people complained about.

Problems in getting programming became legendary.

Satellite dish owners (and I am one) can tell you about scrambling of the signal and what problems that engendered.

Cities have described their powerlessness to address abuses in their area because of tough renewal standards.

The industry became more concentrated and less competitive. Nearly forty percent of all cable subscribers are served by only two cable operators.

Now, Mr. Chairman, the record for cable, although blemished, is not wholly unsatisfactory. As the cable industry has matured and developed, many positive benefits have accrued. Our constituents enjoy more programming diversity. The number of channels per system has increased. Cable has been a strong competitor of network television and the film producing industry. Americans have more video programming choices than any other country in the world. Cable's contribution to this state of affairs has been substantial, and we cannot, certainly we should not, overlook that.

These hearings will help us in many ways. We will hear about some of the problems and some of the things that can be done to solve them. The cable industry has an opportunity to state its case. When these hearings end, we will be more informed and know better what is the right thing to do.

OPENING STATEMENT BY SENATOR BREAUX

I want to commend Chairman Inouye for scheduling oversight hearings on the cable television industry. A number of key issues need to be addressed, including large cable rate increases to consumers, the near-monopolistic control of programming, the quality of services offered by some cable system owners, and increasing industry concentration, i.e., a lack of effective competition.

According to one study, the average fee for Basic cable fare in Louisiana in 1986 was about $9; three years later, in 1989 that average is nearly $16, an average increase of more than 70 percent. Rates in Shreveport, according to the study, jumped from about $5 to nearly $17, an increase of over 200 percent. If these amounts are accurate, cable TV consumers in my state have ample reason to complain, even as they continue to subscribe to cable TV services.

I encourage the committee to take a careful look at the control of market power in the cable TV industry. We have recommendations to restrain, or roll back, market power concentration by restricting the market shares of existing cable systems. We are also encouraged to establish effective inter-industry competition. The telephone industry would welcome the opportunity to compete. Direct Broadcast Satellite TV and satellite dish systems developers are struggling to establish viable subscriber bases. There may be other market de-concentration options as well.

We certainly ought to be concerned with television access in rural America. One or more of the options I have already mentioned may be particularly effective for those rural consumers who are still limited to one or two TV channels after 30 years of service. Let's work for universal equal access to quality television programming.

To some extent, the cable industry may be a victim of its own success. Its educational, news, and sports programming have proven to be enormously attractive. Americans urban and rural want cable, but they want it at a fair price. I am hopeful that we resolve these issues in ways that will encourage continued growth of the kind of positive programming diversity that Americans have found and love in cable television.

I thank the Chairman for initiating these hearings that should provide the basis of solutions to these problems. I must remind the Chairman, however, that cable TV is only a part of the national communications policy that the committee needs to address.

There is still the matter of telecommunications policy being made in the courts rather in the Congress. At this time when changing technology is dictating the way people and nations live and work, I am again urging this committee to further examine the impact of Judiciary telecommunications policy-making. We have abdicated our responsibility to give policy direction in an area with vast potential as an incubator of technological expansion. And, we are doing this at a time when we should be most vigorously and most doggedly pursuing technological growth!

Again, I applaud the Chairman for having these hearings on such an important subject. I believe that the Committee's findings will serve to benefit our economy, and individual consumers in Louisiana and across the Nation.

Senator INOUYE. Now that we've heard about mud wrestling and scorched earth and 117 percent rate increases, may I call upon Mr. Mooney, Mr. Malone, and Mr. Robbins.

Gentlemen, I thank you very much for joining us this morning. I would call first on Mr. Mooney.

STATEMENT OF JAMES P. MOONEY, PRESIDENT, NATIONAL CABLE TELEVISION ASSOCIATION

Mr. MOONEY. Thank you, Mr. Chairman.

We have submitted an extensive prepared statement on the wide variety of issues in which the Committee has expressed interest.

We also know there will be an array of other witnesses before the Committee today and tomorrow, and we ask permission to comment in writing on other testimony the Committee will be hearing these two days.

Senator INOUYE. May I assure one and all that your prepared statements will appear in the record, and, furthermore, that I will accept any comment, addendum, or supplement that you may have following the hearings.

Mr. MOONEY. Thank you.

Senator GORE. Mr. Chairman, could we have the same courtesy afforded the Mayors to comment in writing on what the cable witnesses say?

Senator INOUYE. Oh, certainly. That is for all witnesses.

Senator GORE. Thank you.

Mr. MOONEY. Mr. Chairman, I just want to make a few broad points on what has happened in cable since the Cable Act was passed in 1984 and rate deregulation went into effect at the end of 1986.

First, we have, as everyone knows, experienced a period of post-deregulatory adjustment in basic rates. According to the GAO, the average price of basic service most people subscribe to rose from $11.70 to $14.77 during the first 23 months of deregulation.

This represented a 26 percent increase from December, 1986 through October, 1988.

Basic service, of course, is only one component of most subscriber bills. The average monthly subscriber bill itself, what GAO calls the bottom line, went from $21.58 to $24.68 over the same period, a 14 percent increase.

Now this, of course, occurred not in a vacuum, but in the historical context of basic rates having been held way down during the 14 years the FCC authorized city councils to regulate these rates.

From 1972 through 1986, when deregulation took effect, our basic rates ran 72 points behind the CPI. Had we simply run with the

CPI, from 1972 up to the present, our basic rates would be higher than they are now—about $16.50.

In other words, we have not tried to recapture at all.

The second point I should make is that there has been a direct nexus between cable deregulation and improved cable programming.

I think it is generally admitted today, even by the broadcast networks, that cable is real TV and no longer amateur hour TV.

This has been a direct function of more money put into programming. A Roper poll conducted for one of the broadcast industry organizations earlier this year showed that the public now believes cable programming, with the exception of local news, to be superior to that found on conventional television.

There is a reason for this.

Cable operators' spending for basic programming has increased from about $300 million in 1984 to nearly $1 billion this year, and the investment is noticeable on the screen. Moreover, we give the average subscriber 32 channels today, as compared to 27 channels in 1986, and the average cost per channel to the subscriber has remained virtually flat—46 cents today versus 44 cents three years ago.

Third, there is reason to believe that the spurt in basic rates which occurred in 1987 and 1988 was just as I have described it—a post-deregulatory adjustment.

According to the Bureau of Labor Statistics, cable subscriber bills have flattened out in 1989. The BLS's overall CPI figure for the first nine months of 1989 was up 3.7 percent. But the cable component was up only 2.3 percent.

This suggests that we are now back in line with the general consumer economy, and with one caveat—program costs are still rising—I see no reason why the overall industry won't stay there.

Mr. Chairman, I would close with the observation that we understand full well that we have our problems up here. Customer service has been a problem for us as our subscriber levels have risen rapidly, and some cable operators unquestionably have taken imprudent advantage of their freedom to set rates.

But we don't think the record shows the industry overall to have acted irresponsibly, and we are working very hard to continue to exercise restraint on rates, to further improve the product, which is specialty television, and to make real, perceptible, measurable improvements in our customer service operations.

In short, we are trying to behave responsibly on rates while cleaning up our problems. We hope we will be allowed to do so.

Thank you, sir.

[The statement and questions and answers follow:]

STATEMENT OF
JAMES P. MOONEY
PRESIDENT AND CHIEF EXECUTIVE OFFICER
NATIONAL CABLE TELEVISION ASSOCIATION

Mr. Chairman and members of the Committee, my name is James P. Mooney. I am President and Chief Executive Officer of the National Cable Television Association. NCTA represents more than 2,700 cable television systems, serving 80 percent of the more than 50 million cable households in the United States; it also represents 56 cable programming services engaged in creating and distributing a broad range of programs for cable television.

NCTA appreciates the invitation to appear before you today and welcomes the opportunity to discuss developments in the cable industry since passage of the Cable Communications Policy Act of 1984. The Act has had a positive impact on the development of the television industry in the United States and has fostered competition among broadcasters, cable television operators, and videotape distributors. It has benefitted the public by providing consumers with a wide variety of quality television programming at reasonable cost. It has also spurred the cable industry to invest in the development and installation of new technology.

Congress passed the 1984 Cable Act in part to "assure that cable communications provide and are encouraged to provide the widest possible diversity of information services and sources to the public."[1] The cable industry is fulfilling that promise and is an important part of our nation's telecommunications infrastructure, both in terms of programming and delivery systems. However, the industry is still expanding to meet the needs of the American public, and not all phases of that growth have been smooth. You may be assured that the cable industry is sensitive to the

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1/ P.L. 98-549, sec. 601(4).

problems that exist and that it is striving to provide a level of customer service commensurate with the high quality of its programming. The industry is also working to keep rates reasonable, and I am pleased to report that for the first 9 months of 1989, the CPI increased 3.7 percent while cable rates rose only 2.3 percent.

In this statement, I will (1) review the political and historical events that led Congress to recognize the need for a comprehensive and uniform national policy for cable television; (2) discuss the major provisions of the Cable Communications Policy Act of 1984, both in terms of what Congress intended and how judicial and municipal regulatory actions have influenced implementation of the Act; and (3) survey the impact that this landmark legislation has had on the television industry and the way that cable television serves the American public.

Mr. Chairman, I will demonstrate that despite the industry's growing pains, cable is an excellent value and a benefit to the consumer. Specifically, I will show that:

* Cable is a regulated industry and is subject to a wide variety of local controls, public service obligations, and review by local authorities and the FCC. For example, it is the only communications industry with statutory requirements to enforce equal employment opportunities and the privacy rights of its customers.

* In 1986, basic rates were deregulated where cable systems were subject to effective competition. A GAO study found that average basic rates increased from $11.70 per month in 1986 to $14.77 in 1988, an

increase of 26 percent over two years. Total monthly bills, including premium services, rose from an average of $21.58 to $24.68, an increase of 14 percent over two years. However:

- basic service rate increases have gone hand-in-hand with decreases in the cost of premium services;
- most of the rate increases observed between 1986 and 1988 represented "catch up" for rates that had been held artificially low since 1972, when the FCC first allowed cable systems to import distant signals;
- the average monthly basic service rate of $14.77 in 1988 is still $1.77 below what the 1972 basic rate would be today if it simply had kept pace with inflation;
- basic rate increases have been matched by an increase in the average number of channels received by the subscriber. The GAO found that the average cost per channel has remained at approximately 45 cents since rates were deregulated in 1986.

* Basic service subscribers now receive an average of 32 channels for 50 cents a day--the cost of one issue of USA TODAY. No other industry in America provides such a wide array of information and entertainment at such low cost.

* Cable operators have made a significant investment in programming, bringing material to the public that had often not been available before. Moreover, the structure of program offerings has been simplified for consumers.

* Public satisfaction with cable programming is high and subscribers prefer it to broadcast programming in nearly every category, including entertainment, education, sports, culture, and children's television.

* Cable has become an effective competitor in the video industry, as Congress intended.

* Vertical integration in the industry has been beneficial and has led to an increase in the amount and quality of programming available to the consumer. Vertical integration has not led to discrimination in favor of operator-owned programming nor has it meant that system operators exclude programming in which they do not have a financial interest.

* Horizontal consolidation: ownership in the cable industry is not highly concentrated as measured by either the Herfindahl-Hirschman Index or the four firm concentration ratio.

* Franchise fees are a significant source of general revenues for local authorities and may be spent for any public purpose.

* NCTA agrees with this Committee's desire to reinstate must carry and will not object if the Committee imposes reasonable limits on commercial time in children's television programming.

I. THE HISTORY OF THE CABLE TELEVISION INDUSTRY

The history of the cable television industry has been intertwined with regulation. Cable began in 1948 as a service to individuals in mountainous and geographically remote areas who could not receive over-the-air television signals. It served as a local or "community" antenna service that picked up broadcast signals and distributed them by coaxial cable to subscribers for a fee. The first cable television systems were small local ventures, and these systems still represent an important segment of the cable industry.

As cable developed in its early years, municipal involvement was generally limited to authorizing the use of local streets and rights-of-way and to adopting regulations to protect the safety of life and property. These first cable television franchises or licenses were generally granted upon the application of a prospective operator. In 1952, cable systems were operating in 70 communities and serving 14,000 subscribers. By 1955, community antenna television, as cable was known then, had 150,000 subscribers on 400 systems.

In order to expand from remote areas into areas where over-the-air television signals could easily be received, however, cable operators had to provide potential subscribers with something more, something different than the fare of local broadcasters. As cable began to offer programming alternatives, the line was crossed between cable service as a means to provide mere broadcast retransmission and cable as an alternative to broadcast network programming.

The real catalysts in cable's conversion from an antenna service into a competitive source of programming were the development of satellite technology and cable's entrepreneurial willingness to pioneer that technology as a means for national distribution of made-for-cable programming. In 1975, Time, Inc. invested approximately $30 million and began satellite distribution of Home Box Office (HBO), which until then was distributed primarily over its Manhattan cable system. According to the prevailing wisdom of the "experts" at the time, the move was risky and would not return significant revenues. However, by 1978, HBO had over one million subscribers on almost 400 cable systems, and the era of premium cable programming was born.

Similarly, in 1978, Viacom, another major cable operator, began satellite distribution of Showtime as a competitive alternative to HBO. It later acquired both MTV and Nickelodeon, cable networks devoted to music videos and children's programming, respectively. Both of these services were in financial difficulties when they were acquired, but their formats showed great promise for alternative programming, and Viacom was prepared to nurture its investment patiently.

Following the lead of Time, Viacom, and others -- most notably, Turner Broadcasting -- the cable industry has developed unique cable programming that offers the public quality alternatives to the network sitcoms and soap operas offered by one of cable's television competitors, the broadcasters. In effect, the risk taken by Time, Inc. paid off and changed both the nature and mix of television programming.

Since 1975, the cable television industry has proven that television consumers will pay for distinctive, quality programming not offered by broadcast networks and independent stations. In the process, cable has created a new economic structure in the world of television. As part of this new structure, cable networks assumed financial risks when success was not assured. In fact, some programmers, such as CBS, tried to develop cable programming networks but failed.

Currently there are 65 cable programming networks distributed nationally and 38 cable programming networks distributed regionally -- 103 networks in all. Almost thirty additional networks are in development and may become available to cable consumers. The American public has never before had access to such diversity of viewing choices, thanks to vigorous competition between the cable and broadcast television industries. While broadcast networks still capture more than a 50 percent audience share among cable subscribers, fifteen years ago that number was 98 percent. As cable invests in new, better, and more diverse programming, we expect this trend to continue.

A. Initial Federal Regulation of the Cable Industry

As cable developed into a full-fledged competitor in the television market, regulatory policies governing cable's activities often lagged behind — and actually constrained — progress. The Communications Act of 1934 gave the Federal Communications Commission jurisdiction over interstate communications by wire or radio. Prior to the Cable Act, however, cable proved to be a regulatory conundrum for the Commission. Cable provided television programming to consumers, but did not use the airwaves to do so. This rendered inapplicable any federal licensing scheme based upon the spectrum scarcity rationale that is used by the Commission to support its regulation of broadcast television. On the other hand, cable's use of wire to deliver television programming was not a common carrier transmission service that would allow cable to fit neatly within the FCC's Title II regulatory framework.

Federal regulation of cable began in earnest in the 1960s. In response to cries from broadcasters for protection against potential competition from cable's importation of distant broadcast signals into the service areas of local television stations, the FCC decided that it had the authority to regulate television programming carried by cable systems as a natural and necessary extension of its authority to regulate broadcast television. In 1966, the Commission found that importation of distant television signals could "destroy or seriously degrade the service offered by a television broadcaster," causing reduction in service to households not served by cable systems. In order to protect local broadcasters, the Commission promulgated rules requiring cable systems to carry the signals of all local stations in their areas, to refrain from duplicating programs of local television stations carried on the system during the same day that such programs were broadcast by local stations, and to limit importation of distant broadcast signals into the service areas of local television broadcasters in the top 100 markets.[2]

2/ CATV, 2 FCC 2d, 725 (1966).

Over time, the FCC, in its eagerness to protect broadcasters from competition, went so far as to prohibit cable from purchasing the rights to display movies that were more than three or less than ten years old. Likewise, a cable operator could be fined if he telecast games involving a sport which had been shown by a broadcast station in the same community within the previous two years. As for syndicated programming, a broadcaster's exclusivity contracts were permitted to forbid entirely program retransmissions by cable.

The Commission's authority to regulate cable's broadcast signal carriage practices was challenged and eventually affirmed in 1968 by the United States Supreme Court in United States v. Southwestern Cable Company. The Court held that the Commission had jurisdiction under the Communications Act of 1934 to promulgate such regulations, but the Court warned that the Commission's authority was "restricted to that reasonably ancillary to the effective performance of the Commission's various responsibilities for regulation of television broadcasting."[3]

In reaching its decision, the Court found that "CATV systems perform either or both of two functions. First they may supplement broadcasting by facilitating satisfactory reception of local stations in adjacent areas in which such reception would not otherwise be possible; and second, they may transmit to subscribers the signals of distant stations entirely beyond the range of local antennae. As the number and size of CATV systems have increased, their principal function has more frequently become the

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3/ Ibid., at 163.

importation of distant signals."[4]

At the time, the use of satellite technology was unheard of in the cable industry, and cable had not yet begun to compete vigorously against broadcasters with alternative made-for-cable programming. Nevertheless, the Supreme Court's decision in Southwestern had the effect of relegating cable to second-class status in the television industry. Cable would be allowed to grow, but only if the revenues of local broadcasters were protected.

After the Southwestern case, the Commission became deeply involved in the regulation of cable, promulgating rules that covered nearly every facet of a cable system's operations. The courts, however, became increasingly impatient with the Commission's expansion of regulation.

In 1972, a deeply divided Supreme Court returned to the question of federal jurisdiction over cable. At issue were Commission rules which required cable systems with more than 3,500 subscribers to engage in the local origination of programming. The Court could not reach a majority, but Chief Justice Burger, in providing the swing vote to establish a plurality, stated: "Candor requires acknowledgement, for me at least, that the Commission's position strains the outer limits of even the open-ended and pervasive jurisdiction that has evolved by decisions of the Commission

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4/ Ibid., at 163.

and the courts. The almost explosive development of CATV suggests the need of a comprehensive re-examination of the statutory scheme as it relates to this new development, so the basic policies are considered by Congress and not left entirely to the Commission and the courts."[5]

Despite the Chief Justice's warning to the Commission and his plea for Congressional resolution of cable issues, our industry was caught in a widening spiral of new and burdensome federal regulations. In addition to the local origination rules, the Commission issued rules requiring all cable operators in the top 100 television markets to: (1) develop a minimum capacity of 20 channels; (2) develop the technical capability for accomplishing two-way, non-voice communications; (3) allocate separate channels for use by public, educational, local government, and leased access users, with at least one channel reserved for each; and (4) provide production equipment and facilities for public access use. The Commission also regulated the charges that could be imposed on access users.

At last, the Court had had enough. In 1979, in the second Midwest Video case, the Court ruled that access requirements, which could not be imposed on broadcasters, could not be imposed on cable systems either. "The Commission may not regulate cable systems as common carriers, just as it may not impose such obligation on television broadcasters. We think the authority to compel cable operators to provide common carriage of public-originated transmissions must come specifically from Congress."[6]

5/ U.S. v. Midwest Video, 406 U.S. 649, 676 (1972).

6/ FCC v. Midwest Video, 440 U.S. 689, 709 (1979).

B. Initial Municipal Regulation of the Cable Industry

The Court's invalidation of the FCC rules in the second Midwest Video case represents the high water mark of federal regulation of cable television. Unfortunately, it did not mark the beginning of an era of regulatory restraint vis-a-vis cable. Rather, it was the point at which municipal, rather than federal, regulation of cable television began its ascendancy.

In 1975, the Commission had announced a program of "deliberately structured dualism" in which state and local public authorities ("franchising authorities") were given responsibility to select cable franchisees, establish franchise boundaries, regulate the construction of cable facilities, and maintain rights-of-way. Franchising authorities were allowed to regulate rates for basic service. The Commission retained exclusive jurisdiction over all operational aspects of cable systems, including signal carriage and technical standards.[7]

Franchising authorities moved quickly to fill the regulatory vacuum left by the Commission's diminished presence resulting from the Supreme Court's 1979 decision. The increase in local regulatory activities came at a time when many major cities were deciding which cable companies should be awarded initial franchises to construct cable television systems and provide cable television services. During this period, local public officials viewed cable, in the words of former New York Mayor John Lindsay,

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7/ Cable Television Report and Order, 36 F.C.C. 2d 207.

as "an urban oil well." Not only did cities seek to require cable systems to provide a wide range of "community services," but local officials sought to tax cable operators, in the form of franchise fees, thereby providing city governments with a significant new source of revenue. The rush of prospective cable operators to serve the cities was used to extract valuable and costly considerations wholly unrelated to the provision of cable television service.

The litany of excessive demands placed on cable by local governments formed a large part of the record which led Congress to pass the Cable Communications Policy Act. Similarly, Congress took note of the not-always-judicious willingness of cable operators to agree to such demands. Neither aspect of this record need be repeated here. It is sufficient to recall that the franchising process had created a situation of over-regulation that demanded payments by cable operators in terms of money, services, and facilities that bore little relation to the marketplace or consumers' interests. Regulatory one-upsmanship between cities became the order of the day, and each franchising authority imposed a different set of rules and obligations on its cable system. These terms often reflected political considerations, not economic conditions or consumer demand, as each city council tried to improve on the achievements of its predecessor.

We had come to a situation where the interests of municipal regulators, cable system owners, and potential cable customers differed sharply. Accordingly, in an increasingly competitive market for video distribution, Congress recognized that the time had come to set reasonable parameters on municipal regulation in order to allow cable to get on with the business of serving the American television audience.

II. THE CABLE COMMUNICATIONS POLICY ACT OF 1984

In the 97th Congress, Senator Barry Goldwater of Arizona sponsored S. 2172, prototype legislation establishing cable as a part of the national telecommunications policy. This bill was reported out of the Senate Commerce Committee in 1982, but Congress adjourned sine die before it reached the floor. S. 2172 was supported by NCTA and just as vigorously opposed by the National League of Cities (NLC).

A. The Negotiations Between The National Cable Television Association and the National League of Cities

The Chairmen and members of the House and Senate Commerce Committees and their Telecommunications Subcommittees brought the NLC and NCTA together into negotiations that resulted in a compromise adopted by the boards of both organizations in March of 1983. This compromise served as the blueprint for the Cable Communications Policy Act of 1984. The NCTA-NLC negotiations took place against a backdrop of marketplace, regulatory, and judicial events that worked in unique combination to make Congressional resolution of cable issues desirable, if not imperative, for both the cable industry and the nation's cities.

For the cable industry, the major incentive was the simple fact of a competitive marketplace: the competition for television viewers' time and attention had become too intense for cable to compete successfully while continuing to cope with all of the regulatory burdens imposed by municipal governments. City control of rates, program service offerings, and renewal hindered cable operators in their ability to identify and respond to changing consumer demands. City control of basic programming services forced operators to provide programming in complicated, costly multiple tiers and not, as cable customers preferred, in a single, attractive package. Uncertainty about renewal also discouraged operator investment in new plant and services. Rate regulation kept the cost of basic service artificially low. This in turn kept the cost of premium pay services such as HBO and Showtime artificially high since they had never been within the jurisdiction of municipal regulators.

In addition to these regulatory constraints, cable faced increasingly intense competitive pressures. Videocassette recorders were becoming as commonplace in homes as television sets and stereos, and Hollywood decreed that video rental stores would be allowed to distribute their movies a full six months before HBO and Showtime could acquire them. At the same time, the FCC was taking steps to preempt and deregulate alternative distribution technologies, such as backyard dishes, MMDS, and SMATV.

For the cities, the major incentive to negotiate with NCTA was a desire to preserve the regulatory structure they had created. Pending lawsuits were challenging the cities' right under the First Amendment to grant franchises and their right to regulate cable at all.[8] At the same time, the FCC was showing renewed interest in enforcing its preemptive policies.

The Commission had a long-standing rule that franchising authorities could only assess franchise fees in amounts sufficient to offset the costs of administering the franchise. As a general rule, fees could not exceed three percent of annual gross revenues. Franchising authorities were not allowed to assess higher fees without a specific waiver from the Commission. Waivers for fees of up to five percent were permitted only where a city demonstrated that the actual costs of regulation warranted them. In addition, cities were forbidden from using franchise fees for any municipal purpose other than overseeing and regulating the franchise.

Despite these rules, local authorities across the country often demanded and received franchise fee payments of five percent without securing the required waiver from the Commission. This kind of disregard for federal preemption by franchising authorities was not unusual. Franchising authorities could place cable operators between Scylla and

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8/ The cities' apprehension over these lawsuits was justified a year later when the United States Courts of Appeals for the Ninth Circuit and the D.C. Circuit each found that the First Amendment prohibited cities from limiting franchises so long as pole space for more wires was available. See Preferred Communications v. Los Angeles, 754 F. 2d 1985 (9th Cir. 1985), affirmed, 106 S.Ct. 2034 (1986). Telecommunications of Key West, 757 F.2d 1330 (D.C. Cir. 1985). Ultimately, the Supreme Court remanded the Preferred case to the trial court for further development of a record. The constitutional issue raised by the decision of the Ninth Circuit was not addressed by the Supreme Court and the issue remains unresolved to this day.

Charybdis by forcing the operator either to submit to these demands or claim protection under federal preemption. By asserting this federal protection, however, cable operators risked retribution in rate regulation, packaging changes, renewal, or any of the other regulatory controls commonly exercised by municipalities.

The situation began to shift in 1982 and 1983. The city of Miami demanded from its cable operator a franchise fee of five percent of revenues, plus $200,000 per year in cash for public access, plus in-kind payments for support of access, plus $200,000 per year for the police department's drug education program. The cable operator took the unusual step of bringing the matter to the Commission. The Commission denied the city a waiver and voided all liability for payments over three percent of revenues because the city could not show that the additional money was needed to cover the costs of regulating the franchise. Because franchise agreements that contravened the preemptive policies of the Commission were common (but after the Commission's decision in the Miami case were ultra vires and of no effect), cities were anxious to reach an agreement with the cable industry which could be translated into legislation that would preserve the commitments they had obtained.

The boards of directors of NCTA and the National League of Cities (NLC) adopted a comprehensive compromise agreement in the spring of 1983. The settlement covered a broad range of cable-related issues. At its core was agreement on four central points: (1) the rates and program offerings of basic services carried on cable systems subject to effective competition would be deregulated; (2) franchise renewal proceedings would be constrained by federal guidelines, with a right of appeal to the federal courts; (3) cities would retain authority to choose cable franchisees, mandate facilities (including access facilities), and collect franchise fees of up to five percent of gross revenues without regard to the cost of regulation; and (4) all existing franchise commitments would be preserved unless they violated an express limitation. Although the dynamic tensions within the NCTA and NLC called for constant adjustments, the fundamental principles of the compromise held and served as a foundation for the Cable Act. (The legislative history and, in particular, the court decisions that influenced the Act's treatment of rate deregulation, are discussed on pages 28-37.)

B. Basic Provisions of the 1984 Act

The Cable Communications Policy Act of 1984 represented a watershed in the history of cable television. The statute established a comprehensive national regulatory scheme designed to ensure that the cable industry would be allowed to develop in an atmosphere free from unnecessary and economically burdensome government regulation.

In reviewing the Cable Act, it is useful to categorize the Act's specific provisions into three general areas: (1) the provisions which guarantee the cities' power to continue regulating cable; (2) the provisions which were necessary to limit city regulation in order to allow cable to compete in the video marketplace; and (3) the public interest obligations which are unique not only to the Cable Act, but to cable as a major competitor in the video marketplace.

1. Provisions Which Allow Continued Municipal Regulation

The Cable Act reaffirmed municipal regulation of the cable industry. Despite widespread perceptions to the contrary, the cable industry continues to be subject to extensive controls. Some of our critics, such as the independent broadcasters and MMDS operators, who allege that cable is "unregulated," would undoubtedly protest if Congress considered imposing similar obligations on them.

a. Franchise Selection

In affirming municipal regulation of cable, the Cable Act codified the FCC's policy of deliberately structured dualism. The Act assured that the selection of a cable system operator and the decision of how many cable franchises to award would remain a matter of local regulatory authority. This provision should be underscored. Many of our critics allege that cable is a monopoly because only one franchise exists in most cities. The ability to grant more than one franchise always has been a city's decision, and, under the Cable Act, continues to be so.

Quite frankly, many early franchise awards were made to only one operator because the city required so many commitments that only one franchise could survive economically. Some cities maintain that it is unrealistic to grant more than one franchise, that cable is a natural monopoly, and that competition between two cable systems is not feasible. Whether or not those cities are right, it is a self-fulfilling prophesy.

At the time of selecting an initial franchisee, cities had the option of establishing an environment that would encourage market entry by more than one operator. But most cities did not make that choice. Instead, they moved toward requiring elaborate facilities and plant, access facilities and funding, free telecommunications services for local government, and other requirements that cost operators millions of dollars and discouraged market entry by other operators.

Prior to passage of the Cable Act, the ability of municipalities to franchise cable systems was in jeopardy on a number of fronts. In addition to First Amendment concerns raised in various lawsuits, municipalities faced another vulnerability, especially in awarding a single franchise among multiple bidders. This vulnerability flowed from a Supreme Court decision that found municipalities subject to antitrust liability for restraint of trade.[9] One of the concessions of the cable industry in the cable/cities agreement was acquiesence by the NCTA to legislation sought by the cities in the 98th Congress [10] which eliminated damages in municipal antitrust cases. With the Cable Act, Congress provided cities with further insulation from antitrust liability by creating a regulatory framework for cable franchising that carried at least an implication of immunity. (Section 621 expressly provides that a franchising authority may award, consistent with the Cable Act, one or more franchises within its jurisdiction.)

9/ Community Communications Company v. City of Boulder, Colorado, 455 U.S. 40 (1982).

10/ P.L. 98-544.

b. Franchise Fees

The Cable Act's provisions on franchise fees were another of the major gains for the cities and, correspondingly, another of the major concessions by the cable industry. Cities around the country stood to lose millions of dollars each year if the FCC were to become vigorous in enforcing its three percent franchise fee ceiling and preemption powers. (Recall the discussion earlier about the FCC's ruling on franchise fees in the Miami case.)

The Cable Act raised the fees a franchising authority could impose on a cable operator during any twelve month period from three percent to five percent of gross revenues, a 67 percent increase over the FCC's rule. Further, the Act eliminated the requirement that fees be assessed and disbursed only as needed to offset the costs of regulation; the Act allowed cities to use franchise fees for any purpose. The Act also defined the types of payments which are included and excluded in determining the franchise fee, essentially codifying prior FCC rulings.

The Act allows cable operators and franchising authorities to agree to prepay or defer payment of franchise fees as long as the sum of the fees paid during the term of the franchise does not exceed the amount of money which lawfully could have been collected if the fees had been paid on an annual basis, taking into account the time value of money. This provision essentially grandfathered millions of dollars that had been required as "upfront" payments by some cities, but which were illegal under federal law when they were agreed to.

Under the Act, cable operators may pass through to customers any increase in the amount of franchise fees and must pass through to customers any decrease. Cable operators may also itemize the franchise fee separately on customer billings. This seemingly innocuous provision is one of the most pro-consumer provisions in the Act. Franchise fees are, in fact, a tax on cable service. But local control of cable at the time of the Act was so complete that operators typically were forbidden from informing customers that a percentage of their monthly bills did not pay for cable, but went directly to the local government. Some cities are still uncomfortable with the idea of accepting accountability for this tax and have sought to keep it hidden. Nevertheless, the purpose of the statutory limit on franchise fees was to put a cap on all assessments, other than general taxes, which a franchising authority could impose on cable systems.

Prior to the Cable Act, the FCC had resolved franchise fee disputes under its regulations limiting franchise fees. NCTA believes it was the intent of Congress that the FCC should continue to utilize its expertise to resolve such disputes. Immediately following passage of the Cable Act, however, the FCC declared that the legislation removed its jurisdiction over both pending and prospective franchise fee disputes. After a judicial appeal brought by cable operators faced with assessments in excess of the five percent limit, the FCC agreed to render decisions in franchise fee disputes which were pending when the Cable Act became law.[11]

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[11] 11/ Yakima Valley Cablevision v. FCC, 794 F.2d 737 (D.C. Cir. 1986).

With respect to post-Cable Act disputes involving additional assessments by cities, the FCC adopted a policy of partial forebearance. The FCC reversed its initial decision and found it had jurisdiction concurrent with the courts over franchise fee disputes, but stated it would exercise such jurisdiction only where such disputes impinge on national policy concerning cable communications and implicate the agency's expertise. The appellate court held that, without more express direction from Congress, such forebearance was within the FCC's discretion.[12]

c. Other Municipal Regulatory Authority

As noted earlier, there is a widespread misconception that the Cable Communications Policy Act of 1984 totally deregulated the cable industry. Such an interpretation, however, does not survive even a cursory inspection of the Act.

In addition to the franchise selection and franchise fee powers discussed above, the Cable Act grants franchising authorities the ability to:

i. award or deny renewal of a cable system franchise, subject to federal guidelines;

12/ ACLU v. FCC, (D.C. Cir. July 17, 1987).

ii. require the construction of cable system facilities, including channel capacity, either as part of the initial franchise or during a renewal proceeding;

iii. require cable systems to provide channel capacity, facilities, and equipment for public, educational, and governmental access use (PEG), during either the initial franchising process or franchise renewal proceedings;

iv. establish rules and procedures for the use of channels dedicated for public, educational, and governmental access purposes;

v. prohibit or restrict the offering of programming over channels dedicated for commercial use if, in the judgment of the franchising authority, that programming is obscene, or is in conflict with community standards in that it is lewd, lascivious, filthy, indecent or otherwise unprotected by the Constitution of the United States;

vi. enforce a cable operator's agreement to provide particular facilities and equipment and broad categories of video programming or other services;

vii. enforce requirements contained in any franchise prior to enactment for the provision of services, facilities, and equipment, whether or not related to the establishment or operation of a cable system;

viii. regulate rates for basic cable service in markets where effective competition does not exist;

ix. require and regulate the installation or rental of equipment which facilitates the reception of basic cable service by hearing impaired individuals;

x. assure that the opportunity to purchase cable service will not be denied to any class of citizens because of income or economic status;

xi. require customer service requirements of the cable operator in granting a franchise;

xii. enact and enforce consumer protection laws consistent with the Cable Act;

xiii. review the operator's customer service performance in judging a renewal application.

d. Preservation of Franchise Commitments

The last major concession which the cable industry made in order to strike a compromise with the cities preserved franchise commitments that cable operators had made prior to the Act. This concession is one of the most important, although frequently overlooked, provisions of the 1984 Act.

We have already discussed how the franchise process and its attendant regulatory regimes spun out of control and ignored limitations that had been imposed on franchising authorities through FCC preemption. In addition to exceeding their authority to regulate the operation of cable systems, cities were notorious in demanding commitments from cable operators to finance various municipal projects that were wholly unrelated to the provision of cable television service.

Throughout the legislative process that led to passage of the Cable Act, the cable industry was called upon to make concession after concession to dissident cities that wanted to undo the agreement. More often than not, the city in question was less interested in the public policy issues under consideration and more concerned that the extensive concessions it had obtained from its cable operator might be taken away. Accordingly, Section 624 and Section 637 of the Act work in tandem to assure cities that cable operators must comply with all of the commitments made at the time of their franchises unless they contravene express limitations contained in the Cable Act or fall within the type of commitments that qualify for contract modification under Section 625.

2. Cable Act Provisions Which Allow Cable to Compete in the Video Marketplace

A second major category of elements included in the 1984 Act was designed to give cable the ability to compete effectively for the video consumer. Indeed, one of the express purposes of the Cable Act was to "promote competition in cable communications and minimize unnecessary regulation that would impose an undue economic burden on cable systems."[13] In order to accomplish this purpose, it was necessary for Congress to establish orderly guidelines for the exercise of federal, state, and local authority with respect to regulation of cable systems. The Cable Act provides jurisdictional allocations, regulatory limitations, and due process guarantees in a number of crucial areas. This section will review three provisions of the 1984 Act that were designed to enable cable to compete in the video service industry: (a) deregulation of basic rates and program service offerings; (b) franchise renewal; and (c) contract modification.

a. Deregulation of Basic Rates and Program Service Offerings

Probably the most contentious provisions of the Cable Act are those which deregulate basic service rates and grant freedom to repackage — or retier — programming services. Rate deregulation was a principal feature of Senate and House legislation from the time of introduction to the time of enactment. The specifics of rate deregulation changed, however, as the bills moved through the legislative process. It is important to recall the regulatory situation that existed before 1984 in order to appreciate fully the evolution of these provisions.

13/ Section 601(b).

i. Background: Municipal Rate Regulation

In 1969, the FCC limited municipal control of cable rates to must carry (off-air broadcast) signals and public, educational, and governmental (PEG) access channels.[14] The Commission specifically preempted cities from controlling the rates of any other programming service. Consequently, cities never had jurisdiction to regulate the rates for pay television, including premium channels such as Home Box Office, Showtime the Disney Channel, and other services generally offered to cable customers on an "a la carte" basis. Although the occasional franchise authority would assert regulatory jurisdiction over premium channels, for the most part cities understood that price control of these premium networks was beyond their jurisdiction.

The problem was somewhat different with respect to another form of pay television, the so-called basic cable networks delivered by satellite. These networks are supported in part by advertisers and are generally offered by cable operators as a part of the basic service tier. CNN, Headline News, ESPN, USA Network, Arts & Entertainment, Nickelodeon, and other services are examples of these basic cable networks.

Although the FCC's rate preemption policy was intended to encourage the development of such services, the cities took advantage of the fact that cable operators often had adopted a marketing strategy, still popular today, of offering these services together with local broadcast signals and

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14/ First Report and Order, FCC Docket 18397, 20 FCC 2d 201 (1969).

PEG channels for a single package rate. The problem arose when the cities claimed regulatory jurisdiction over all programming not offered on a per-program or per-channel basis instead of just the domain allowed them by the FCC (must carry and PEG).

Municipal control over rates often had less to do with reasonable prices for consumers than it had to do with cities using their authority to influence the cable operator. Cities were astonishingly open about this fact. For example, Seattle Mayor Charles Royer, then President of the National League of Cities, in testimony before the House Subcommittee on Telecommunications, Consumer Protection, and Finance, stated unequivocally: "In most cities, rate regulation is used as a tool for enforcement."[15]

ii. Legislative History of Rate Deregulation

From the cable industry's perspective, freedom from rate regulation was a necessary and principal objective for legislation if cable was to become truly competitive. Rate deregulation was one of the cornerstones of the NCTA/NLC compromise, and remained so when the parties were expanded to include the U.S. Conference of Mayors.

15/ Statement of Charles Royer, Mayor of Seattle, Washington, for the National League of Cities, Hearings before the Subcommittee on Telecommunications, Consumer Protection and Finance, Committee on Energy and Commerce, House of Representatives on H.R. 4103 and H.R. 4229, 98th Cong. 1 Sess., serial no. 98-73, May 25, 1983.

Rate deregulation, as passed by the Senate in S. 66, was originally slated to occur in markets where four full power television station signals were available (including each of the major networks) and after a transition period of five years or half the remaining life of the franchise, whichever was greater. New systems and renewed systems in markets with four signals were to be deregulated immediately. These rate deregulation provisions of S. 66, as passed by the Senate Commerce Committee on April 27, 1983, formed the baseline from which all subsequent changes in both House and Senate rate deregulation provisions occurred.

S. 66 provided that: "Cable franchises which are in existence on the date of enactment and which meet the test for rate deregulation; that is, four television signals are present, shall have the deregulation of basic rates deferred for a period of 5 years or for a period equal to one-half of the remaining term of the franchise, whichever is greater."[16] Again, systems built or renewed after the effective date would be deregulated immediately.

In the meantime, the bill provided that "[a]ny regulated rate may be increased annually by the cable operator by up to 5 percent or the regional consumer price index (CPI) for the preceding 12 months, whichever is greater."[17] This increase would be automatic, and elective at the option of the cable operator; the franchising authority could not

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16/ Senate Report No. 98-67, 98th Cong., 1st Sess., p. 22.

17/ Ibid.

interfere. Further, cable operators were given the discretion to increase rates automatically for basic service beyond the five percent or CPI limit if the operator made a request for an increase and it was not acted upon by the franchising authority within ninety days.[18]

Before the Senate passed S. 66 on June 14, 1983, Senator Lautenberg secured two perfecting amendments. The first amendment allowed local authorities to reregulate basic service rates once subscription rates exceeded eighty percent of homes passed, based on the assumption that adequate off-air reception was not available.[19] The second amendment eliminated the provision allowing for an automatic five percent rate increase at the discretion of the cable operator, thereby tying rate increases that did not have municipal sanction to increases in the regional CPI for the preceding twelve months.[20]

During Senate consideration of S. 66, Senator Dixon offered an amendment which would have eliminated even this discretionary increase. The Senate defeated the amendment by a vote of 72 to 26. In doing so, it became clear — as it did during other portions of the debate -- that the Senate fully intended to deregulate basic cable rates where there was effective competition as defined in the bill.[21]

18/ Ibid.

19/ See Cong. Rec. June 13, 1983, S 8257.

20/ Ibid.

21/ Cf. Cong. Rec. June 13, 1983 S. 8257-8258; Cong. Rec. June 14, 1983 S. 8305-8306, 8316-8318.

Senator Packwood explained: "All this bill does now, so far as these rates are concerned, is simply to say that, one, local cable may have its rates go up no greater than the regional consumer price index, and two, that where they compete in an area where the viewers can receive at least four other over-the-air signals clearly, three of which must be network, there will be no rate regulation." [22]

In the House bill, H.R. 4103, the Telecommunications Subcommittee adopted the Senate's approach and conditioned rate deregulation on the presence of four over-the-air signals. Prior to consideration of the bill by the full House Energy and Commerce Committee, however, two major events occurred to force reconsideration of the terms for rate deregulation.

First, the Commission acted on a petition, filed by the cable operator in Las Vegas, Nevada, who was being prevented by the city from retiering some satellite signals out of his basic service offering. In what came to be known as the "Nevada" decision, the Commission issued a declaratory ruling in which it clarified the extent of its preemptive policies. The FCC said that local franchising authorities, regardless of franchise provisions or contract language, could not prohibit a cable operator from placing distant broadcast stations or satellite-delivered cable programming networks on non-basic service tiers.[23] In other words, under FCC preemption policies, the multiple tier regulation, common at the time

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22/ Cong. Rec. June 14, 1983, S. 8314.

23/ Community Cable TV, Inc., 95 FCC 2d 1204 (1983), reconsidered 98 FCC 2d 1180 (1984).

throughout the cable industry, was ultra vires and unenforceable by the cities. Cable operators were free to remove these programs from basic service packages, as market forces dictated, and reprice them as market forces allowed.

The second major event which shaped the Act's rate deregulation provisions was a Supreme Court decision. Just prior to the House Energy and Commerce Committee's markup of H.R. 4103, the U.S. Supreme Court ruled on Capital Cities Cable v. Crisp,[24] a case which struck down an Oklahoma statute prohibiting, among other things, cable transmission of out-of-state commercials for beer and wine. The Court affirmed the FCC's plenary jurisdiction over cable. In its discussion, the Court specifically singled out and appeared to affirm the FCC's action in the "Nevada" decision.

In light of the "Nevada" decision and the Crisp ruling, the proposed cable legislation appeared to be more regulatory than the status quo. In response, the full House Energy and Commerce Committee sought to make the Act's deregulatory provisions more compatible with existing law. Although multiple tier regulation would be allowed to continue during the transition period, that period was reduced from five years or half the remaining life of a franchise to a straight four years. (Ultimately, it was reduced to two years.) Similarly, because the FCC's preemptive policy applied to all cities, the Committee decided to increase the number of markets in which deregulation would occur. This issue was extremely sensitive for the cities and rather than define "effective competition" in the statute as less than four signals, the Committee accepted the recommendation of NCTA, the NLC, and the Conference of Mayors to allow the FCC to determine where cable was subject to effective competition for basic service. Cable systems in places meeting the FCC's standard would then qualify for deregulation.

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[24] 467 U.S. 694 (1984).

After the original NCTA/NLC compromise was ratified by their respective boards in 1983, it became necessary for the cable industry to make a continuous string of concessions in order to appease dissident cities and maintain the fragile agreement. Following the "Nevada" case and the Crisp decisions, the pendulum swung the other way, and cities -- fearful of further erosion of their regulatory regimes -- were forced to make last minute concessions to cable to maintain the agreement.

During House consideration of H.R. 4103, it became quite clear that Members considered the compromise negotiated by the National League of Cities, the U.S. Conference of Mayors, and NCTA to be a series of tradeoffs in which the primary benefit for cable was rate deregulation after a two-year transition period. Some may argue that Congress somehow did not really intend to fully deregulate the pricing of cable services or that Congress wanted the criteria for effective competition to be set so stringently that many cable systems would remain subject to rate regulation. Yet, in the wake of "Nevada" and Crisp, and the NLC/USCM/NCTA 1983 compromise, the legislative debate on H.R. 4103 makes it clear that Congress intended, and understood, that H.R. 4103 would effectively deregulate the pricing of cable services.

As the bill's principal sponsor, then-Congressman Timothy E. Wirth explained to his colleagues, "[H.R. 4103] deregulates the rates charged for basic cable services in two years, allowing the marketplace to dictate the price for cable programming and services."[25] Later in the debate, he stated: "H.R. 4103 as amended before us today reduces the four-year transitional period for municipal rate regulation which was in the bill, to two years. In addition, the bill provides that cable systems which have retiered or repriced cable services in reliance upon the FCC's Nevada decision cannot be required to restore, retier, or replace such services where the change in price or tiering occurred as of September 26, 1984."[26]

Other Members were equally clear in their understanding. For example, Congressman John Bryant described the major features of the legislation: "The cities get continued rate regulation for two years and a guaranteed five percent franchise fee. Cable operators, on the other hand, have assurance that they will not be unfairly denied renewal of their franchises and, after the two-year transition period, will be able to set rates to reflect market forces and competition."[27]

Similarly, Mr. Nielson: "Mr. Speaker, I am happy to support the bill... We now have deregulation of the cable industry while at the same time giving additional revenue to the cities and also retaining local

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25/ Ibid., H. 10436.

26/ Ibid., H. 10436.

27/ Ibid., H. 10444.

rights to control over obscenity."[28]

Mr. Tauzin: "Let me also say that in my own city of New Orleans there is a battle going on between the city council and Cox Cable that is in court today. This bill, as I understand it, would guarantee to the city at least two more years of basic regulation that would not disturb at all the court challenges that are going forward."[29]

The House passed H.R. 4103 on October 1, 1984, and sent it to the Senate. The Senate added a number of amendments, including a provision that made it clear that cable systems already deregulated under state law would remain deregulated during the two-year transition period.

As the legislative history specifically points out: "In all other respects, the Senate adopts the House provisions in Section 623 on the deregulation of rates."[30] With its amendments, the Senate adopted the Cable Act by unanimous consent, after which it was returned to the House and approved by that body.

iii. Section 623 - Regulation of Rates

Section 623 of the Act prohibits government regulation of cable television system rates except where the cable system is not subject to effective competition, as defined by the FCC. Where a cable system is not

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28/ Ibid., H. 10444.

29/ Ibid., H. 10445.

30/ Cong. Rec. October 11, 1984, S. 14285.

subject to effective competition, rate regulation is limited to the rate charged for basic cable service. However, Section 623 allows franchising authorities in all markets to prohibit discrimination among customers of basic service and to regulate the installation and/or rental of equipment facilitating reception of cable service by hearing impaired individuals.

The Cable Act provided for total rate deregulation in competitive markets after a two-year transition period for franchises in existence at the time of the legislation's enactment. Franchises entered into and renewals granted after enactment in competitive markets were barred from regulation ab initio. In non-competitive markets, however, basic service could be regulated.

In addition, the Act required the FCC to continue its oversight of cable television rates and competition in the marketplace. The FCC must report its findings to Congress by 1990, along with any recommendations for legislative changes. We understand that the Commission is beginning this process now.

iv. The FCC Rulemaking to Implement Deregulation

In 1985, the FCC conducted its rulemaking proceeding to define "effective competition," as instructed by Congress through the Cable Act. Essentially what Congress had posed to the Commission was an economic question answerable by empirical evidence: at what point does the presence of broadcast signals in a market impose a competitive discipline on the price of basic cable service?

Despite the empirical nature of the task assigned to the Commission, most of the comments submitted to the Commission during its rulemaking process were philosophical, with many arguing that cable is a video distribution monopoly (a concept specifically rejected in the Cable Act), while others argued that cable should be regulated because it was subordinate or ancillary to broadcasting (another concept rejected by Congress in the Cable Act). NCTA submitted extensive econometric analysis which indicated that the presence of no more than three broadcast stations will serve as a competitive restraint on pricing of basic cable service. No other empirical data were submitted by any party to the proceeding.

Perhaps the most surprising comments came from the National League of Cities. As we noted above, the FCC's decision in "Nevada" and the Supreme Court's apparent affirmation of that preemption in Crisp led the cities to agree to more immediate and comprehensive deregulation than that contained in the original S. 66 and in H.R. 4103 as approved by the House Energy and Commerce Committee.[31] The transition period to rate deregulation was set at two years in the statute, and it was the understanding of all parties to the compromise that the definition of effective competition would be limited -- as it always had been — to the presence of off-air signals and that the requisite number would be less than four. Despite that fact, the National League of Cities urged the FCC to define effective competition as the presence of five off-air signals, including each of the networks, an independent, and a PBS station, plus the presence of an alternative medium of communications in that system's market that could provide virtually every other programming service offered by the cable operator. In other words, under the NLC's proposal to the FCC, almost no cable system in America would have been deregulated.

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[31] See discussion of S. 66, which originally set a four station standard, on pp. 30-33, and the House Energy and Commerce Committee's decision to set a "less than four" standard, p. 35.

The FCC correctly read the intent of Congress to deregulate basic cable rates in markets where basic cable service is subject to effective competition from broadcasters. In its rules, the Commission defined effective competition to basic cable service as the presence of three unduplicated broadcast signals in a market.

Several parties appealed the FCC's ruling, but the Court of Appeals for the D.C. Circuit largely upheld the FCC's rate deregulation order and the three signal standard.[32] Several cities asked the Supreme Court for review, but on March 21, 1988, the Court denied certiorari.[33]

The one part of the FCC's rules that was not affirmed by the Court, but was remanded for further proceeding, dealt with how the Commission would measure the presence of off-air broadcast signals and the manner by which franchising authorities could contest assertions of signal availability by cable operators. On March 24, 1988, the FCC amended its rules to require that at least three off-air signals must be available in 100 percent of the community served by a cable system in order for these to be considered effective competition.

32/ ACLU v. FCC, 823 F.2d 1554 (D.C.Cir. 1987).

33/ Connecticut v. FCC, 108 S. Ct. 1220 (1988).

v. The Cities' Response to Deregulation

In addition to their effort to rewrite the definition of effective competition at the Commission, some cities have sought to undermine the implementation of rate deregulation. Some franchising authorities have tried to persuade cable operators to "waive" their rights to rate deregulation, but the courts have not permitted such end runs around federal law. Moreover, some cities have attempted to argue that rate freeze provisions do not constitute rate regulation under the Cable Act and thus prevent even an operator subject to effective competition from raising rates. These interpretations have also been rejected by both state and federal courts.[34]

b. Section 626 - Franchise Renewal

In addition to deregulation of rates and services, the Act sets forth standards and procedures in Section 626 governing the renewal of cable franchises. This section was not intended to displace informal negotiations for renewal between cable operators and local franchising authorities. However, the protections of this section may be invoked by either the franchising authority or the cable operator to govern the renewal process. Its purpose is to provide an orderly, reasonable and fair process for considering franchise renewals.

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[34] 34/ See e.g., Town of Westwood v. Adams Russell Company, Inc., 507 N.E.2 763 (Mass App. Ct. 1987). See also, City of Dubuque v. Group W Cable, Inc., Case No. C-85-1046, N.C. Iowa (June 18, 1986).

Once invoked, Section 626 requires the franchising authority to commence public proceedings for the purpose of identifying future cable-related needs and interests of the community and to review the performance of the cable operator under the current franchise. Upon completion of these proceedings, the incumbent operator may (on his own initiative) or must (at the request of the franchising authority) submit a renewal proposal which contains such material as the franchising authority requires, including a proposal for an upgrade of the facilities of the cable system. Upon submission of the renewal proposal, the franchising authority has four months either to grant renewal or to issue a preliminary assessment that the franchise should not be renewed. In the event that the franchising authority wishes not to renew the franchise, and upon the request of the cable operator, it must conduct public hearings to consider: (1) whether the operator has substantially complied with the material terms of the existing franchise; (2) whether the quality of the operator's service has been reasonable in light of community needs; (3) whether the operator has the financial, legal, and technical ability to provide the services, facilities and equipment set forth in its renewal proposal; and (4) whether the operator's renewal proposal is reasonable to meet the future cable-related needs and interests of the community, taking into account the cost of meeting such needs and interests.

During this renewal proceeding, the cable operator is entitled to full due process rights, including the right to adequate notice, the right to introduce evidence and compel the production of evidence from others, the right to examine witnesses, and the right to a hearing record. The franchising authority must base its decision solely upon the record of the proceeding and must issue a written statement of the reasons for its decision. In the case of a denial, the decision must be based upon the above four standards. However, a franchising authority may not deny renewal of an operator's franchise for failure to comply substantially with the material terms of the existing franchise unless the operator has been given notice of and an opportunity to cure the non-compliance, or if the franchising authority has waived its right to object or has acquiesced in the non-compliance. Finally, the Act provides standards for judicial review of any proceeding wherein a cable operator's renewal proposal has been denied.

The renewal provisions of the Cable Act have afforded much-needed stability for cable operators who have provided good service and want to keep doing so. This stability, which was altogether absent before the Cable Act, changed the incentive for a cable system from recouping its investment within the term of a single franchise to reinvesting in better programming, better facilities, and better community services.

c. Section 625 - Contract Modification

As noted earlier, the Cable Act preserved all provisions of pre-Cable Act franchises, unless they violated express limitations in the Act. At the same time, however, Congress took notice of the fast-changing competitive conditions confronting cable and built in some latitude, albeit quite limited, for adaptability where necessary.

In addition to all existing contract remedies, the Cable Act established an optional procedure by which cable operators may seek modification of service, facility and equipment commitments. Facility and equipment requirements are to be modified upon a showing of "commercial impracticability," a relatively difficult test. Service commitments, other than public, educational, and governmental access service, may be modified upon a showing by the operator that the mix, quality, and level of service required by the franchise would be maintained under the new arrangement.

These provisions have been used to undertake negotiations with franchising authorities who might otherwise have refused to bargain. If contract modification negotiations are unsuccessful, the operator may go to court. Very few instances of litigation have occurred. The Court of Appeals for the Fourth Circuit in Tribune v. Montgomery County, Maryland determined that franchising authorities may not impose fines or penalties on a cable operator who is currently seeking relief under the contract modification provision of the Cable Act.[35]

35/ Tribune United Cable v. Montgomery County, MD. 784 F.2d 1227 (4 Cir. 1986).

3. Cable Act Provisions Which Set Forth Cable's Public Interest Obligations

The Cable Act stands as a legislative landmark in national communications policy in large part because the cable industry joined with Congress in taking the unprecedented step of recognizing, in federal statute, its public interest obligations. In this section of my testimony, I would like to discuss four specific public interest obligations that the Act spells out for the cable industry: (1) equal employment opportunity; (2) public, educational, and government access (PEG); (3) cable channels for commercial use; and (4) privacy.

a. Section 634 - Equal Employment Opportunity

Section 634 of the Act prohibits discrimination in employment on the basis of race, color, religion, national origin, age, or sex. This section requires cable operators to establish, maintain and execute a continuing program of specific practices designed to ensure equal opportunity in every aspect of their employment policies and practices. The Act directs the FCC to prescribe rules to carry out the intent of Section 634. Additionally, cable operators are required to submit a copy of their EEO policies to the Commission.

The Act also requires operators to file with the FCC, on an annual basis, a statistical report which identifies by race and sex the number of employees in several specified job categories. On the basis of these filings, the FCC annually certifies cable systems to be in compliance with the EEO requirements. Not less than once every five years, the FCC is required to investigate and review the employment practices of each individual cable operator. The FCC is empowered to impose forfeitures on any cable system which fails to comply with the requirements of the Act. Willful and repeated violation of the EEO provisions can also jeopardize an operator's ability to obtain renewal or transfer ownership of the system.

Mr. Chairman, no other industry in communications has agreed to a similar, specific statutory obligation. The cable industry recognizes its obligation to pursue equal employment opportunity. We did not oppose inclusion of these provisions in the Cable Act because we believe that equal employment opportunity is not an imposition -- it is our responsibility.

b. Section 611 - Public, Educational and Governmental Access (PEG)

Under the Cable Act, franchising authorities may, in new or renewed franchises, require that reasonable channel capacity be dedicated for public, education or governmental access channels. The franchising authority must set rules for allowing a cable operator to offer programs over unused PEG channels. However, the cable operator may not exercise control over the content of PEG programming.

In many communities, PEG access has met and surpassed expectations. In others, it has not enjoyed the success that franchising authorities, Congress, and cable operators hoped it would. In these communities, the public has not participated in local program production and people have not watched public, educational, and governmental access channels in any meaningful numbers. All too frequently, access groups continue to require substantial amounts of money for studios, facilities, and technicians when there is little demand for the programming. While some access programming does attract consumer interest, we believe it is generally fair to say that most access programming does not -- and the access requirements of the Act are certainly not cost-free. The fact is that there are numerous cases of franchises granted in the 1980s where the costs of access in payments, equipment, and channel capacity add several dollars to a subscriber's monthly bill.

Access requirements are also beginning to become the subject of litigation and controversy.[36] While there have been a few cases to the contrary, the access requirement has been held to be unconstitutional by a majority of federal court decisions regarding cable franchise provisions.[37] NCTA has not participated in these cases.

36/ For example, some white supremacist organizations are starting to make use of PEG access. In Kansas City, the franchising authority returned the PEG channels to the operator rather than allow the Ku Klux Klan to use them.

37/ Century Federal v. City of Palo Alto, No. C-85-2168 EFL Slip. Op. (N.D. Cal., Sept., 1987); Group W Cable, Inc. v. City of Santa Cruz 669 F. Supp. 954 (N.D. Cal. 1987). A contrary decision was reached on public access provisions in Erie Telecommunications, Inc. v. City of Erie, 659 F. Supp. 580 (W.D. Pa. 1987).

c. Section 612 - Cable Channels for Commercial Use

In addition to channels which must be set aside for public, educational, or governmental use, the Cable Act establishes a federal regulatory regime under which cable operators with 36 or more activated channels must dedicate capacity for commercial use by persons unaffiliated with the cable operator. The number of channels to be set by an operator is based on the operational capacity of the system. Under the Act's provisions, if a person unaffiliated with a cable operator seeks to use a channel for commercial use, the operator is required to establish prices, terms, and conditions for such use which are sufficient to ensure that it will not adversely affect the operation, financial condition, or market development of the cable system. As with public, educational, and governmental access channels, cable operators are denied by statute any editorial control of the programming carried to their customers on commercial use channels.

To date, very few people have availed themselves of these leased access channels. However, the cable industry is ready to honor its public obligations in this regard if and when the demand emerges.

d. Section 631 - Privacy

Another of cable's public interest responsibilities recognized in the Act deals with the right of our customers to privacy. These statutory provisions require cable operators to notify their customers when they sign up (and at least once a year thereafter) of the kinds of information the operator collects about his customers and the sort of disclosures the operator may make of that information. The statute also generally prohibits disclosure of personal information, except under certain circumstances, and requires cable operators to destroy such information when it is no longer needed. Subscribers are given access to information about them and are protected in the event personal information is the subject of a subpoena.

III. TRENDS AND DEVELOPMENTS SINCE ENACTMENT OF THE CABLE COMMUNICATIONS ACT

Mr. Chairman, I have devoted substantial discussion to how regulatory issues raised in conjunction with the Cable Act were worked out, or are being worked out. When it comes time for you to grade the cable industry since deregulation, however, NCTA believes that the principal question should be: how effectively are the interests of American television viewers being served? I think you will find that the Act has produced, and will continue to provide, extremely positive benefits for cable customers.

A. Rates and Program Service Offerings

On December 29, 1986, the two-year transition to rate and packaging deregulation ended; cable operators were free, for the first time, to offer basic cable service subject to market forces rather than local government regulation.

Basic service tiers usually contain, among other channels, local broadcast stations plus satellite-delivered cable channels such as C-SPAN, Cable News Network, and ESPN. Until deregulation, the cost and composition of basic service tiers was regulated in many markets. As one industry analyst noted, "[w]ith basic rates held down artificially by local rate regulation, cable operators lacked freedom to package their services and often had to rely on increases in pay rates to improve the bottom line."[38]

An examination of industry-wide basic service prices clearly indicates that cable operators were, under regulation, pricing their services at artificially low levels. From 1972 to 1986, for example, average industry-wide basic cable rates lagged 72 points behind the Consumer Price Index.[39]

38/ Paul Kagan Associates, Inc., Cable TV Franchising, June 14, 1985, p. 2.

39/ Between 1972 and 1986, basic rates grew by 89.6 percent, from $5.85 to $11.09, while the CPI for all consumer items grew 162 percent from 41.8 to 109.6 (Paul Kagan Associates and Bureau of Labor Statistics, respectively).

1. Pricing Changes Since Deregulation: Looking at the Customer's Overall Monthly Bill

The data available on cable service pricing changes since deregulation indicate that while basic service prices have increased, premium network prices have either decreased or remained unchanged.[40] Moreover, the number of channels which customers receive has expanded and channel line-ups have been redesigned to better reflect the demands of subscribers. Given these variables, the most appropriate measure of cable price changes is the overall monthly bill for cable service, rather than the price change in basic service. This is also the approach taken by the GAO in its recent study of cable rates.

In August 1989, the GAO issued a report requested by the Chairman of the House Subcommittee on Telecommunications and Finance regarding cable television rates and services. The essential findings were that over the first 23 months of cable deregulation, the average price of basic service rose from $11.70 to $14.77, an increase of 26 percent, while the average cable subscriber's monthly bill went from $21.58 to $24.68, an increase of 14 percent. The GAO calls this last number "the bottom line", and says that if adjusted for inflation, it represents an increase of 8 percent in

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40/ According to Paul Kagan Associates, premium network prices have, on average, decreased since deregulation. In December 1986, the average monthly rate for a premium service was $10.31. By December 1988, the average monthly rate was $10.18.

"constant dollars" in the average subscriber's monthly bill.[41]

These numbers are not inconsequential, but given the history of the cable industry, we think they are not unreasonable, for the following reasons:

a. As noted, between 1972 and 1986, when local governments could regulate basic service, cable rates ran 72 percentage points behind the CPI. Indeed, even post-deregulation, the average basic rate is still $1.77 below what the 1972 basic rate would be today if during the intervening years it had simply increased with inflation.[42] Cable operators have not tried since 1986 to recapture everything lost to inflation before then.

b. Cable subscribers are getting a lot more for their money than was the case sixteen years ago, or even three years ago. The GAO reported that the average number of basic channels provided to subscribers rose from 27 channels in 1986 to 32 channels at the end of 1988. The GAO also found that the average cost per cable channel stayed nearly flat, rising slightly from 44 cents per channel in 1986 to 46 cents per channel in 1988.

41/ The GAO also reports that the average price of the "lowest priced basic service" increased 29% over the same period, from $11.23 to $14.48, and that the average number of channels provided as part of this service increased from 24 to 30. As the GAO points out, however, "Since most systems have only one tier of basic service the most popular service is generally also the lowest priced service" (pg. 23).

42/ If the average basic cable rate had increased at the overall inflation rate (based on the CPI) between 1972 and 1988, it would have been $16.54 in 1988, $1.77 higher than the actual rate of $14.77 found by GAO.

c. The added channel capacity provided to basic subscribers reflects in part increased investment by our industry in plant upgrades. In 1986, we spent $246 million to improve existing facilities and add channel capacity. In 1987, that figure rose to $292 million and in 1988, it was up to $417 million, a 70 percent increase in just two years. Moreover, in 1989, the industry is expected to spend $515 million to upgrade cable plant.

d. The quality of cable programming -- something impossible to measure statistically but nonetheless real -- has improved markedly over the past few years. This is a direct result of a 66 percent increase in basic programming expenditures by operators between 1986 and 1988. In 1989, operator expenditures for basic programming will increase another 18 percent, reaching nearly a billion dollars. This investment will be reflected in the quality of the programming provided to our subscribers.

The GAO survey does not depict an industry broadly abusing its pricing flexibility. Cable companies have not attempted to recapture all of the revenues they lost to inflation, and most rate increases have been offset by increased channel capacity and improved program quality. Basic cable remains a good buy for the average family at 32 channels of service for $14.77 a month, which is less than it costs to take a family out to the movies.

Although the GAO study goes no further than last year, the Bureau of Labor Statistics reports that for the first 9 months of 1989, the overall CPI rose 3.7 percent while the CPI for cable rose only 2.3 percent. This very strongly suggests that the post-deregulation adjustment in cable rates is over. From now on, we can hope to see a more normal curve than that experienced in the immediate post-deregulation period.

2. Cable Penetration Has Increased Since Deregulation

Increases since deregulation in the number of homes subscribing to cable are further evidence that the changes in cable prices and service offerings have reached a marketplace equilibrium and have consumer acceptance. Between February 1987 and July 1989, the percentage of U.S. television households subscribing to basic cable service increased from 48.7 percent to 56.4 percent.[43] Similarly, the number of homes subscribing to cable as a percentage of homes passed has also increased since deregulation. In January 1987, cable penetration of homes passed was 56.5 percent,[44] but by October 1989, it had increased to 60.8 percent.[45]

43/ According to A.C. Nielsen data, 42,820,780 of the nation's 87,896,350 television households subscribed to cable television in February 1987. By comparison, in July 1989, there were 50,897,080 households subscribing to cable out of a total of 90,320,300 television households.

44/ Paul Kagan Associates, Inc., Cable TV Programming, December 22, 1986, p. 8.

45/ Paul Kagan Associates, Inc., Cable TV Programming, October 27, 1989, p. 5.

B. Increased Programming and Construction Expenditures Since Deregulation

Since deregulation, the cable industry has been reinvesting its additional revenues to upgrade its service offerings. In particular, the cable industry has substantially increased its investment in cable programming. In 1988, spending by cable systems for basic programming alone was approximately $814 million, almost two and one-half times the $302 million spent in 1984.[46]

This investment means more channels and more options for consumers. In 1984, 57 percent of the nation's cable customers had access to 30 or more channels. Today that figure is 87 percent and climbing.[47] Another recent trend is conversion to addressable converters, a technology that can provide consumers with pay-per-view options. In 1984, only 18 percent of cable households had addressable converters. By the end of 1989, that number will have grown to 38 percent and will rise rapidly.[48] This pattern of increased expenditures to upgrade and rebuild plant is expected to continue.

46/ Estimate of NCTA, based on Paul Kagan Associates, Inc. data.

47/ Warren Publishing, 1989 Television and Cable Factbok, Cable & Service Volume, No. 57, p. C-375; 1984 Television and Cable Factboook, No. 52, p. 1726.

48/ Paul Kagan Associates, Cable TV Technology, October 25, 1988, p. 4.

C. Franchise Fees Produce Substantial City Revenues

The Cable Act has also produced indirect benefits for cable subscribers and nonsubscribers alike. As I noted earlier, one of the cities' major objectives was to raise the federal ceiling for franchise fees and to eliminate restrictions on their use. This provision has provided substantial revenues for cities. Note that none of cable's actual competitors or would-be competitors pay a similar tax to the communities in which they operate.

In 1984, prior to enactment of the Cable Act, municipalities received $200 million in franchise fees[49] and were required to devote the money to administering cable franchises. Since passage of the Cable Act, from 1985 through 1989, cable systems will have paid an estimated $3.053 billion in franchise fees.[50] That money was available for any municipal use. In 1988, cable systems paid $691 million to local franchising authorities while cities received only $275 million from federal Urban Development Action Grants.

50/ Paul Kagan Associates, Cable TV Franchising, June 25, 1986, p. 4.

50/ NCTA estimate based on data from Paul Kagan Associates.

D. Improved Diversity and Quality of Television

A major assumption underlying the Cable Act was that the promise of cable television was not being fulfilled. If a more fair and stable regulatory environment could be established, it was hoped that cable owners would increase their investment in the industry, and thereby improve cable's diversity and quality. Cable is fulfilling its promise by developing and providing a wide range of programming choices for consumers.

With increasing operator investment in programming, it is no surprise that top basic cable networks are expected to spend $945 million for programming in 1989, up by approximately $200 million, or 27 percent, from the amount spent in 1988, and more than double the $382 million spent in 1984, when Congress passed the Cable Communications Policy Act.[51] Attributing improved basic cable programming to the fact that the industry "has more money to spend," Business Week noted that "basic cable channels are looking spiffier" and that "these days cable channels are growing into much, much more than retirement homes for yesteryear's hits."

Perhaps the greatest evidence of cable's success in providing quality has been produced by our principal competition — the broadcasters. Each year, the NAB's Television Information Office commissions the Roper Organization to survey America's attitudes toward television. 1989

51/ Paul Kagan Associates, Inc., Cable TV Programming, July 31, 1989, p. 2

was the first year the public was asked to compare cable television with network television. The result was that cable got better marks than network television for sports, cultural, children's and educational programming, and overall quality. The following chart reports some of the poll's findings.

1989 ROPER POLL (percentages)

	Regular TV	Cable TV	Both the Same	Do Not Know
Better entertainment programming	26	47	16	11
Better national news coverage	45	33	11	11
Better local news coverage	72	11	7	10
More educational programs	28	47	11	14
More sports programming	17	61	10	13
More cultural programming	22	51	10	16
Better quality programs overall	32	37	16	14
Better programs for children	31	39	11	20
Greater program variety overall	24	52	12	12

There is good reason for the public's preference for cable programming. Last year, the TV critics rated the program "Dear America: Letters from Vietnam" as the best program seen on television in 1988; "Dear America" was an original production of Home Box Office. HBO also won two Emmys in 1988 and two Oscars in 1989, all for original productions. Home Box Office continues to develop new and original programming of a caliber seldom seen on broadcast television.

Quality cable programming is not limited to pay channels: it is evident on basic channels as well. The Arts and Entertainment series tracing U.S.-Soviet relations, "The Eagle and the Bear," was compared favorably by The New York Times to the classic documentary, "Victory At Sea." Basic service program networks are tackling difficult issues of the day in a way that the broadcast networks are not. Lifetime has done a serious examination of the growing childcare crisis in the country. The Learning Channel, in conjunction with the U.S. Conference of Mayors, is exploring our nation's drug crisis.

Children's programming continues to be a major priority for cable and a fertile source of quality programming on cable. Shows like "Ask Mr. Wizard" on Nickelodeon, Jim Henson's "Fraggle Rock" on TNT, and The Disney Channel provide education and entertainment for children that is at least as good, if not better, than anything on broadcast television. National Geographic specials are first aired on Superstation TBS, then on broadcast television. The Discovery Channel and The Learning Channel educate and entertain children and adults alike. The litany of quality programming goes on and on.

Aside from the Roper Poll, the broadcasters themselves are paying us a compliment by trying to copy popular cable formats. For example, we now see broadcasters offering home shopping channels and music videos. They even compete against cable with cable's own programming. When Fox launched its network with a Sunday night line-up, it featured "It's Garry Shandling's Show," a weekly comedy series which shows reruns of episodes that have already appeared on Viacom's Showtime.

Not only have cable operators fostered more and better cable programming by investing directly in programming networks, they have also increased the amount of money their systems spend to acquire programming. From 1980 to 1988, the amount of money by cable systems in programming increased by 842 percent, from approximately $276 million to approximately $2.6 billion. I believe the record is clear that cable has now proven that there can be more to television than cops, robbers, and half-hour comedies. In the five years since passage of the Cable Act, more than half of America's television households subscribed to cable television. There is no better affirmation of cable's value and service, since people must pay for cable every month: if they are not satisfied, they can choose to terminate their service at any time.

E. Cable Fosters Competition

Despite cable's success, it has not — as some of our critics claim — dampened competition in television. Indeed, during cable's emergence in the 1980s, there was dramatic growth of new technologies in the television marketplace that spawned vigorous competition and challenged the dominance of the commercial broadcast networks. As a result, the 98 percent audience share that commercial broadcast networks enjoyed ten years ago is now closer to 60 percent, while the total number of television households has increased from under 75 million in 1979 to over 90 million today.

The following facts highlight the growing competition in the television industry:

1. The number of independent television broadcasters has more than tripled to 417, primarily because of FCC policies that promoted the development of UHF broadcasting.

2. Cable television has finished wiring most of the major metropolitan centers of America: there are today more than 9,000 cable systems serving over 50 million households.

3. VCRs are a major means of video distribution, increasing from 1.1 million units owned in 1979 to nearly 60 million in 1989. VCR penetration grew to 65.8 percent of TV households, surpassing even the growth of cable during the 1980s. Hollywood typically releases its movies to videotape outlets before it allows them to be shown on cable.

4. Home satellite dishes, legalized by FCC rules and the Cable Communications Policy Act of 1984, proliferated from less than 800,000 to nearly 2.6 million today.

5. In less than three years, since the FCC began licensing MMDS operators, 26 systems have come into operation with approximately 173,000 subscribers. Another 30 systems have been licensed and should begin service shortly.

All of these trends point to one conclusion: the television marketplace, once ruled by three networks, has become highly competitive. Consumers are reaping the benefit of that competition by gaining access to an unprecedented selection of diverse television programming. The cable industry has led the way in creating and packaging new programming choices for consumers.

IV. Ownership In The Cable Television Industry

There are currently 9,010 cable television systems in the United States, serving approximately 50 million American households. Cable is now available to 88 percent of American TV households and is purchased by just over 60 percent of these homes. Many of the nation's cable systems share common ownership by multiple system operators (MSOs). As these companies have grown in recent years, their size and diversification have attracted significant attention. That attention has fallen largely into two general areas: concern over vertical integration and questions about horizontal concentration. I will discuss each of these in turn.

A. Vertical Integration

1. Extent Of Vertical Integration In The Cable Industry

Vertical integration in the cable industry, i.e., MSO investment in programming networks, has recently come under substantial scrutiny. However, 46 percent of all operational or planned cable networks are not vertically integrated. In those cases where vertical integration has occurred, consumers have benefitted from increased choice and improved quality.

In January 1985, when the Cable Act took effect, there were 43 national satellite-delivered video cable services. Today there are 65 such services, a 51 percent increase. This figure includes attrition of some cable networks that are no longer in business and 47 new starts. In addition, 29 more services are in various states of development and should be available to customers in the near future. Three of the five largest networks (ESPN, USA Network, and CBN's Family Channel), have no operator investment yet have wide distribution. Indeed, from 1979 to 1989, ESPN grew from 4 million subscribers to 51.1 million, USA from 4.8 million (in 1980) to 48.5 million subscribers, and The Family Channel from 7 million to 44.3 million subscribers. Other popular cable networks, such as The Disney Channel and The Nashville Network, also have no cable operator investment. It is interesting to note that among the most popular national cable networks with no operator ownership, USA and Disney are owned by movie companies (MCA and Paramount, and Disney, respectively) while ESPN is owned by a broadcast network (CapCities/ABC).

As the following table demonstrates, of the 65 nationally delivered cable video networks, 29 (45 percent) have no ownership affiliation whatsoever with the operating side of the cable industry. Moreover, 15 (39 percent) of the 38 regional programming networks function with no operator involvement. In addition, of the 29 programming networks that are scheduled to be launched, 17 (59 percent) are proceeding without operator investment.

CABLE PROGRAMMING NETWORKS: NUMBER OF NETWORKS WITH OPERATOR OWNERSHIP/EQUITY AND WITHOUT OPERATOR OWNERSHIP/EQUITY

	Total Number of Networks	Total Number of Networks With Operator Ownership/Equity	Total Number of Networks With No Operator Ownership/Equity
National	65 (100%)	36 (55%)	29 (45%)
Regional	38 (100%)	23 (61%)	15 (39%)
Planned	29 (100%)	12 (41%)	17 (59%)
TOTAL	132 (100%)	71 (54%)	61 (46%)

Further evidence that vertical integration has not foreclosed entry into the programming marketplace is the fact that 10 (31 percent) of the 32 national programming services currently available that have been launched since January 1985, such as FNN/SCORE, have done so without operator involvement.

2. Effects Of Vertical Integration In The Cable Television Industry

Television consumers have benefitted substantially from cable system operator investments in cable programming networks. These benefits can be seen in the greater diversity and better quality programming available to cable customers.

a. Operator Investment In Programming Means More Choice For Cable Customers

It is important to understand that operator investment in programming enables the cable industry to be a more effective competitor in the video marketplace. It has been the MSOs' willingness to invest their revenues in developing new cable programming that has produced a rich and varied menu for American television consumers and transformed the cable industry from a medium used principally to retransmit broadcast signals into one that provides consumers with real programming choices.

For television viewers, cable's vertical integration has led to the creation of:

- Nickelodeon — quality programming for children, an audience that commercial broadcasters have all but abandoned.

- Black Entertainment Television -- the only 24-hour national Black entertainment network.

- C-SPAN and C-SPAN II — the cable industry-funded public affairs channels that provide unique coverage of the U.S. Congress, as well as a wide range of public policy-related events.

- Bravo — a network devoted to award-winning domestic and foreign films and performing arts specials ranging from opera to jazz.

- Turner Network Television (TNT) — programming devoted to family viewing.

- The Discovery Channel — an all-science and nature documentary channel which was preserved by cable operator investments.

- Cable News Network (CNN) and Headline News — the pioneering all-news networks that now set the standard for news reporting.

Investment by cable operators in programming is the result of several factors. The first is need: cable must compete with broadcasters and their networks by producing better programming. One way that cable competes most effectively is by targetting niche markets and creating programming aimed at particular interests or needs among our subscribers. It is somewhat analogous to the market fragmentation that we have seen over the last several years with magazines in which there now seems to be a periodical for every conceivable interest and hobby.

The second major factor behind operator investment is economic necessity. Traditional sources of funding are unwilling to take a risk on specialty programming. Without operator investment, the diverse programming choices enjoyed on cable today would not exist. The further away you get from the mass audience approach of broadcasters -- lowest common denominator programming — the scarcer potential investors are.

Banks will not finance specialty cable networks because they find the risk unacceptable. Traditional sources of programming capital, such as Hollywood studios, have also been uninterested. For example, Warner started MTV and Nickelodeon. When they needed more money to continue developing these channels, they went to other motion picture studios with the opportunity to purchase or invest in the networks, but were turned down. Eventually they sold the networks, along with Showtime, to Viacom, a major cable MSO willing to take the risk.

The Committee has heard this year from Bob Johnson, President of Black Entertainment Television, and John Hendricks, president of the science and education network, The Discovery Channel. Both told of their fruitless efforts to obtain funding from traditional sources. Operator investment in these networks, as in others, has been a matter of capitalization for the network, not acquisition for the MSOs. The operators are minority investors whose level of equity participation in the networks falls far short of control. Without operator investment, neither Black Entertainment Television nor The Discovery Channel would exist today.

The same is true for other programming networks started or maintained with operator funding, e.g., C-SPAN and C-SPAN II, the Weather Channel, CNN and Headline News, VH-I, Home Box Office, Cinemax, The Movie Channel, and Mind Extension University, among others. MSO investment in programming is the engine driving the cable industry to fulfill its potential by developing a wide range of programming choices for consumers.

b. Vertical Integration Has Not Foreclosed The Market To Other Programmers

As I have discussed, Mr. Chairman, the cable industry's investment in programming has greatly expanded the diversity of choices available to consumers. This has not, however, excluded independent cable programmers who are unaffiliated with MSOs from the market.

We believe that the most significant study of this issue to date is one prepared for NCTA by Dr. Benjamin Klein, Professor of Economics at UCLA. This study, "The Competitive Consequences of Vertical Integration in the Cable Industry," was released in June 1989 and was provided to your Committee at the media concentration hearings on June 21st. It may be useful to highlight the results of his study here.

Dr. Klein devoted the bulk of his analysis to a careful examination of whether there have been any negative consequences from vertical integration in the cable industry. His study analyzes the network carriage patterns of a random sample of 400 cable systems that serve 33 percent of all subscribers; he focused on carriage of the 28 largest basic and premium cable networks on these cable systems. Dr. Klein found that vertically integrated MSOs are not using their systems as a tool to exclude competing cable programming networks from the market. His conclusion was supported by the following:

i. No MSO, whether vertically integrated or not, possesses the economic power to exclude potential competitors from program supply. Even the largest MSO (TCI) cannot by itself prevent the entry of a new programming network.

ii. Vertically integrated MSOs are somewhat more likely to carry their own programming networks; however, this effect is very small (less than 3 percent) compared to the channel capacity and programming requirements of the average cable system.

iii. There is no evidence that vertically integrated MSOs systematically exclude programming networks in which they do not have ownership interests. In fact, the four largest MSOs with the greatest vertical integration, TCI, ATC, Viacom, and Cablevision Systems, are generally more likely than non-vertically integrated cable operators to carry the most popular cable networks in which they do not have an ownership interest.

iv. The result is that cable consumers of vertically integrated MSOs have a wider selection of program choice among the most popular cable networks than consumers of non-vertically integrated cable systems.

Dr. Klein stated:

> Vertical integration benefits the viewing public by expanding programming availability while posing no current or likely future threat to competition. This implies a Congressional regulatory response to vertical integration in the cable industry is not necessary. Any anti-competitive effects that arise in the future can be handled on a case-by-case basis by active enforcement of existing antitrust laws. Rigid industry-wide rules to regulate vertical integration in the dynamic cable programming marketplace are likely to be harmful to consumers.[52]

Others have looked at vertical integration in the cable industry and reached similar conclusions. In June 1988, the National Telecommunications and Information Administration released a study, entitled "Video Program Distribution and Cable Television: Current Policy Issues and Recommendations," which found that cable's vertical integration has produced no adverse consequences. While noting that ownership affiliation does increase the probability that a premium network will be carried by affiliate systems, the analysis concluded that "carriage of affiliated services generally does not occur to the exclusion of unaffiliated services."[53]

52/ Dr. Benjamin Klein, The Competitive Consequences of Vertical Integration in the Cable Industry, June 1989. p. 4.

53/ NTIA Report 88-233, p. 102.

The NTIA analysis further tested whether vertically integrated MSOs discriminate against non-affiliated basic services. Although the statistical conclusion reached by NTIA for basic networks was less strong than for pay networks, NTIA found that vertically integrated systems are not likely to discriminate against unaffiliated basic services. Based on these analyses, NTIA concludes that: "In sum, common ownership of cable systems and cable programming services does not appear to affect adversely the supply of cable programming or the diversity of viewing choices for cable subscribers."[54]

In another study, much more restricted in scope than Klein's analysis, Michael Salinger, an associate professor at Columbia's Graduate School of Business, conducted a statistical analysis of whether ATC, a cable MSO owned mostly by Time, Inc. is more likely to carry HBO and Cinemax than Showtime or the Movie Channel (both owned by Viacom), and whether Viacom's cable systems are more likely to carry Viacom's networks than Time, Inc.'s networks. (Salinger did not examine other pay services or any basic networks.) Salinger concluded that ATC and Viacom are more likely to provide the services they own and less likely to provide the services they do not own.

Salinger's results have been interpreted by some to support the position that vertical integration in the cable television industry is harmful. However, Salinger suggested in his study that vertical integration may also provide benefits, such as lower consumer prices.

54/ Ibid.

As Salinger testified before this Committee on June 21st, his analysis does not provide a definite answer on whether the impact of vertical integration in the cable industry is harmful or beneficial.

The logical conclusion of these three reports is that there is no evidence of systematic exclusion of nonaffiliated programming by vertically integrated MSOs. The available research does suggest that vertically integrated MSOs are somewhat more likely to carry networks in which they have an investment. But, as Klein points out, we must ask what this means in practice (see pp. 35-48 of his report).

Dr. Klein found that the incidence of carriage of affiliated networks by vertically integrated MSOs is about three percent higher than carriage of the same network by unaffiliated cable systems. Put in a consumer context, in systems with excess capacity, consumers tend to get an extra channel (which is a program network affiliated with the MSO); on saturated systems, the difference in carriage of affiliated and nonaffiliated programming on vertically integrated MSOs amounts to about one channel.[55] Note that anytime a program network feels aggrieved because it is not carried on a particular cable system, adequate remedies are available under the Communications Act, and in some cases, the antitrust laws.

55/ The additional network carriage figure was derived by multiplying the average number of channels in which the four largest vertically integrated MSOs have an ownership interest (7.8 channels) by 15.3% (which is the percentage by which vertically integrated MSOs are more likely to carry programming in which they have an ownership interest than do systems without an ownership interest in particular networks). Therefore, vertically integrated systems, on average, carry one additional channel of programming in which they have an ownership interest than do non-affiliated cable systems.

When Congress passed the Cable Communications Policy Act of 1984, it established a federal set-aside of channel capacity on systems with 36 or more activated channels; it also gave programmers who were unaffiliated with the cable system's owners the right to be carried on those channels. To date, this federal right has seldom been exercised. It is somewhat difficult to understand the charges that program networks cannot obtain carriage on cable systems without giving up ownership equity to system operators when Congress has already created a remedy for that situation which has gone unused.

C. Vertical Integration and Must Carry

Some broadcasters, mostly independent broadcasters who are unhappy with the extent of their cable carriage or the channels on which they are carried, claim that vertical integration is responsible for non-carriage or "unfavorable" channel positions. Their allegations regarding vertical integration are often accompanied by allusions to a supposed anti-broadcast conspiracy among cable operators. However, these allegations are not supported by any data upon which sound policy can be based nor by any evidence that proves misconduct.

The reason for the broadcasters' problem is simple. Even in the absence of federal regulatory or statutory requirements, cable systems continue to carry the signals of virtually every broadcast television station qualified for carriage under the FCC's last must carry rules.

Moreover, the overwhelming number of broadcast stations are carried on cable channels at or below their off-air number. In short, there is no evidence that MSOs, vertically integrated or not, favor their own networks at the expense of broadcasters.

Last year, NCTA asked the consulting firm of Price-Waterhouse to survey the extent to which local broadcast stations are carried on cable systems and the extent to which their channel assignments have changed since the FCC's last must-carry rules were struck down by the court in December 1987. The 3,966 respondents to NCTA's study served 32.5 million subscribers, or over 69 percent of all U.S. cable customers. Given the high response rate, it is reasonable to assume that the survey accurately portrays the cable industry's carriage of broadcast stations.

Under the FCC's last must carry rules, which were based on a compromise between the National Cable Television Association (NCTA), the Community Antenna Television Association (CATA), the National Association of Broadcasters (NAB), the Association of Independent Television Stations (INTV), and the Television Operators Caucus (TOC), broadcast stations with a threshold audience share that met the definition of "local" were entitled to cable carriage, subject to a cap in each market. Price-Waterhouse reached the following conclusions:

i. 98 percent of the broadcast stations that qualified for carriage under the last must carry rules are carried today, despite the absence of a legal requirement to do so.

ii. 97 percent of the cable systems would still be in compliance with the FCC's last set of must-carry rules if they were still in effect today.

iii. 91 percent of the systems carrying qualified stations reported no channel repositioning of these stations.

iv. 80 percent of the channel repositions reflect stations that were repositioned to cable channels equal to or lower in number than the station's off-air channel assignments.

v. 87 percent of qualified broadcast stations are currently carried on cable channels equal to or lower than than the stations' off-air assignments.

The FCC also conducted its own survey of signal carriage patterns last year which produced comparable results.

Many of the broadcasters complaints about cable signal carriage stem from the insistence of some UHF broadcast licensees (i.e. "high" numbered stations) that they receive preferred channel positions (i.e. "low" VHF channel numbers) on cable systems. Notwithstanding the advent of hand-held remote controls, which allow viewers to go from one channel to another without scanning all those in between, many UHF broadcasters believe that a low-numbered channel position on a cable system is necessary for them to compete against other TV channels, particularly made-for-cable networks. (See my statement on must carry which I submitted to this Committee on October 25, 1989.)

The cable industry's position, however, is that broadcasters and cable operators should be free to negotiate the terms of carriage wherever possible. In cases of disputes, broadcasters should have a legal right to be carried on their FCC-assigned channels, or lower if a cable system does not have sufficient capacity. In other words, channel 33 should not have a statutory right to occupy channel 5 on a cable system, to the detriment of other cable-provided services, such as C-SPAN or CNN. There is no precedent in law for such preferred treatment of UHF broadcasters, nor is it logical or equitable.

As I told the Committee October 25th, NCTA supports a reasonable, constitutional must carry statute. A neutral policy on channel positioning, such as on-channel assignment, could be part of any new must carry law. The FCC could resolve disputes, and pending the FCC's determination of a channel positioning rule, a one-year moratorium on channel shifting would answer the broadcasters' complaints about being "moved around." However, allowing broadcasters unilateral control over channel positioning would likely founder on the same First Amendment shoals that have invalidated not one but two sets of FCC must carry rules. NCTA continues to be willing to work with the principal representatives of the broadcast industry and Congress to produce mandatory carriage rules that will withstand judicial review.

3. Vertical Integration In The Entertainment Industry

Much of my testimony today, Mr. Chairman, has focused on vertical integration in the cable television industry. I have also described the competition we face in the video marketplace. In order to understand the effect of ownership on competition in the cable industry, it is important to understand the ownership patterns of cable's competitors.

An examination of the video marketplace reveals that it is dominated by fewer than a dozen diversified media companies. There are many differences among them, but they share a common trait: each has significant resources, experience, and expertise devoted to the creation, packaging, and distribution of intellectual property.

Of all the competitors in the video distribution market, by far the highest degree of vertical integration is found in Hollywood. The top ten studios (ranked by box office share) control 96 percent of the theatrical film market, 69 percent of the prerecorded videocassette market, and 67 percent of all syndicated television programming. In addition, these ten Hollywood studios supply 60 percent of the broadcast network's prime time programming and are primary suppliers to, or owners of, cable networks. Moreover, the top studios have strengthened vertical integration in their industry by purchasing 11 percent of all U.S. movie theater screens, as well as broadcast stations that serve 28 percent of the total U.S. audience.

The recent efforts by Paramount to effect a hostile take-over of Time, Inc. illustrate an important facet of the debate over vertical integration in the cable industry. One of the most frequent, vocal, and persistent critics of MSO investment in programming has been the Motion Picture Association of America. This criticism is confusing to NCTA because, for years, MPAA attacked cable's compulsory license as parasitic. Now that MSOs are investing in their own programming, and now that this programming is rated by consumers as the best on television, MPAA does not want the competition. However, as you know, Mr. Chairman, MPAA's concerns about vertical integration are limited to cable operator investment in programming and do not appear to extend to vertical integration in the motion picture industry or the acquisition of cable systems by major studios.

B. Horizontal Concentration Of Ownership In The Cable Industry

Some of cable's competitors have voiced concerns about consolidation in the cable industry. However, according to standard measures the cable industry is not a highly concentrated industry.

The two prevailing measures of market concentration are the top four firm concentration ratio and the Herfindahl-Hirschman Index (HHI). The top four firm concentration ratio simply measures the percentage of the market captured by the four largest companies in that market. The Herfindahl-Hirschman Index reflects the market share distribution among all firms in a given market, giving proportionately greater weight to the market shares of the larger firms. Although the Justice Department has chosen the HHI as the appropriate measure in determining whether or not a market is concentrated, both approaches are extensively used.

A market is considered concentrated when one firm, or a small group of firms, has a sufficient share of the market to exercise power over it. The Department of Justice, and prevailing economic theory, consider this market power to exist when the four firm concentration ratio reaches 50 percent, or when the HHI reaches 1,000.[56]

Current data on the market share of the cable operators that own a multiple number of local cable systems (MSOs) show low levels of concentration. Applying the HHI index to the top 20 cable MSOs, the resulting HHI value of 467 falls well below the DOJ's threshold of 1,000.[57] Thus, according to this measure of market consolidation, the cable industry is far from being concentrated.

56/ U.S. Department of Justice Merger Guidelines, p. 18. Note that the HHI threshold of 1,000 is a minimum level of concentration. The maximum HHI level attainable is 10,000, which represents a pure monopoly situation (one firm with 100 percent of the market = 100 x 100).

57/ In its guidelines, the DOJ states that although it is desirable to include all market firms, small fringe firms do not affect the HHI significantly and are therefore not critical. Only the Top 20 MSOs were used here because beyond the 20 largest MSOs, each smaller MSO captures less than one percent of the market, and thus the square of a number less than one will have little impact on the value of the index. The top 20 MSOs serve approximately 33 million subscribers, or about 65 percent of the nation's subscribers.

Using the four firm concentration ratio, the conclusion is the same. According to the most recent data available, the top four cable MSOs have attained a 35 percent share of the cable market, a share far lower than the 50 percent threshold that defines a concentrated market.

V. PROGRAM DISTRIBUTION AND EXCLUSIVITY

Mr. Chairman, there is no evidence that vertical integration in the cable industry has foreclosed the market to non-affiliated cable networks. NCTA also believes that vertical integration has not foreclosed the development of competing technologies.

1. Competition in the Video Marketplace

Competition in the distribution of video programming generally occurs between media within a discrete geographic market. As I described earlier, the cable television industry was largely an extension of the broadcast television industry until the late 1970s. Cable was little more than a retransmission service for broadcasters, providing a quality picture where the ability to receive that same signal over-the-air was not optimal. Cable did not become a competitor in the video marketplace, in any meaningful sense of the word, until it began to develop its own programming alternatives to the fare available from broadcast stations.

There can be little disagreement that CNN and Headline News compete directly with the broadcast networks' news operations; that Arts and Entertainment and the Discovery Channel compete against programming typically found on PBS; or that ESPN competes against sports programming carried by broadcasters. Furthermore, the cable industry has found it highly effective to compete against broadcasters by serving market segments ignored by television stations. Black Entertainment Television, Nickelodeon, children's programming networks, and Spanish-language networks allow cable operators to compete against local broadcasters by serving interests in the community which the latter have largely ignored or abandoned.

2. Exclusivity and Federal Law

Product differentiation is the key to successful competition in the distribution of video programming. Exclusivity over product is usually the best means to protect diversity, which is why programmers want to determine how and by whom their products are to be exhibited. Federal law has long recognized that by protecting exclusive rights to intellectual property, one enhances competition and provides for increased diversity of information and entertainment. Indeed, federal policy has recognized that disruption of these exclusive rights works against, not toward, competition.

For example, federal law does not mandate that a local movie theater or even a national chain of theaters is entitled to show any particular movie. It does not mandate that all television stations are entitled to network affiliation agreements, nor does it forbid a network-owned broadcast station from being programmed with the same network's "feed." It is recognized, for example, that NBC may license its wholly-owned and operated broadcast station in Washington, D.C. (WRC-TV) as the only distributor of NBC programming in the Washington area, to the exclusion of other aspiring NBC affiliates. Moreover, federal law does not permit a cable system to use its compulsory license to import network programming over the objection of a local affiliate of that network.

The federal government recently took steps to strengthen broadcasters' exclusive rights to programming. On March 21, 1989, the FCC issued an order which will reinstate syndicated exclusivity for broadcasters; federal policy will therefore not permit cable to use its compulsory license to import programming from distant stations if a local station has the complete rights to a market for such programming. At the same time, the FCC broadened the network non-duplication rules by expanding the situations where local broadcast network affiliates can prevent carriage of distant broadcast network affiliates.[58]

58/ It must be noted that NCTA believes this particular set of rules, as fashioned by the Commission, will be largely unworkable for cable operators and will be difficult for consumers. These particular rules will confuse, frustrate, and anger consumers when popular programs and out-of-town

(Footnote continues on next page)

Finally, just last year, Congress recognized the need to protect program exclusivity in the Satellite Home Viewer Act of 1988. That law extends a compulsory license to satellite carriers to make broadcast signals available to home satellite dish owners. Congress restricted that license, however, so that home dish owners may not receive network programming via satellite if they have access to a terrestrial broadcast affiliate of that network. The law also ordered the FCC to see if similar protection for non-network programming is feasible.

3. Exclusivity And "Competing" Technologies

Some satellite dish dealers and MMDS operators, who have seen the rising popularity of cable programming, now maintain that they would like to "compete" with cable by selling its programming. This, of course, comes after cable networks and cable operators have taken all of the risks to develop the programming and establish its brand name identity. Some groups have come to Congress and demanded that cable networks be stripped of their ability to determine how to distribute their original product. These groups want cable networks, and only cable networks, to be statutorily deprived of their exclusive right to distribute their own programming.

(Footnote continued from previous page)

stations are dropped. NCTA opposed the imposition of these rules when the FCC began its proceedings in 1987 and we continue to believe these rules are anti-consumer. Notwithstanding our strong and consistent opposition, however, NCTA has decided not to protract the dispute further. It should also be noted that NCTA detected no real support in Congress to challenge these rules. Accordingly, the Board of Directors of NCTA voted April 6, 1989, to refrain from joining appeals to the D.C. Circuit to invalidate the FCC's new syndicated exclusivity rules.

These proponents of "competition" are not proposing to expand the diversity of programming options in the marketplace nor to provide consumers with more entertainment and information. Rather, they simply want a federal warrant for cable programming, an approach that violates the principle of protecting one's intellectual property rights.

4. Availability Of Cable Programming Networks To MMDS Systems And Home Satellite Dishes

Some MMDS operators and satellite dish dealers have alleged that vertical integration in the cable industry has led MSOs to force cable networks to withhold programming from their technologies. While some individuals may not have distribution contracts for the particular networks they might wish to sell, Dr. Klein's study demonstrates that cable networks are generally available to MMDS systems and the dish community.

According to Dr. Klein, MMDS systems currently carry a total of 42 cable program services. Furthermore, all of the top 10, and 22 of the 28 most popular basic and premium networks, are sold to MMDS systems. Contrary to some claims, MMDS systems do offer their subscribers program services which are among the highest-rated and most popular cable networks available, including ESPN, Superstation TBS, HBO, CNN, Nickelodeon, Lifetime and MTV.

The Committee is already familiar with the availability of cable networks to home satellite dish owners. In its report to the last Congress on S. 889, the "Satellite Television Fair Marketing Act," the Committee found: "The evidence presented at the hearing demonstrated that scrambled signals of cable programming are being made available to dish owners at prices comparable to those being charged cable subscribers. At the hearing, there was no dispute that all of the cable programming services that scramble now distribute their programming to dish owners. In addition, according to the FCC and the National Cable Television Association, there are over 70 program services that are not currently scrambled."

Not only is cable programming available to the home satellite dish market, it is available at prices equivalent to or lower than those charged to cable subscribers. According to Paul Kagan Associates, the average price of basic cable service for cable subscribers is $14.45 per month and the cost of cable-delivered basic service plus a premium network channel, such as Showtime, is $24.71 per month. Similarly, packages of basic programming networks comparable to what cable subscribers receive (such as the packages offered by Viacom Satellite Network) are available to dish owners for as little as $13.25 per month. Basic service packages, plus a premium network such as Showtime, are available to dish owners for as little as $18.75 per month, far lower than the corresponding price which cable subscribers pay.

QUESTIONS OF SENATOR INOUYE AND THE ANSWERS OF MESSRS. MOONEY AND ROBBINS

1. It has been suggested that the franchise renewal process needs to be revised to permit the franchising authority to take into consideration factors such as ratemaking history, employment practices, character qualifications, and ownership of other media interests. What is your opinion?

With the Cable Communications Policy Act of 1984, Congress established "franchise procedures and standards which encourage the growth and development of cable systems and which assure that cable systems are responsive to the needs and interests of the local community" (PL 98-549, sec. 601(2)). The Act reaffirmed the cities' right to grant franchises and set forth standards by which cable companies would be judged when they applied for renewal or new franchises. The goal of the bill was to make explicit the powers of cities and the rights of cable operators in the franchising/refranchising process, thus guaranteeing due process for all participants.

Under the Cable Act, cities and other franchising authorities have the power to determine:

(1) the terms and conditions for public, educational, and governmental access channels on cable systems;

(2) how many franchises will be awarded;

(3) franchise fees up to 5 percent of a cable company's gross revenues;

(4) how these franchise fees will be spent;

(5) requirements for a cable system's facilities, equipment, and channel capacity at the time of renewal or initial construction if new;

(6) customer service obligations and construction schedules;

(7) basic cable rates where the FCC determines that there is no effective competition from other video services.

The Act also imposes obligations for subscriber privacy and equal employment opportunity on all cable systems. Finally, it ensures that operators whose rates are deregulated are not immune from EEO and other non-discrimination obligations (s. 623(f)).

With regard to refranchising, the Cable Act established clear standards for reviewing an operator's application for renewal. It also guaranteed public review of a community's future cable-related needs and the performance of cable operators under existing franchise agreements by establishing guidelines for:

(1) the submission of proposals for renewal;
(2) adequate and prompt public notice;
(3) public hearings;
(4) timely action on the proposal (within 4 months);
(5) full and fair participation by all interested parties, including the right of cable operators to introduce evidence and compel the production of evidence;
(6) written transcripts and written decisions;
(7) appeals to the court for relief in the event that a city does not follow the Act's renewal procedures or if its decision is not supported by a preponderance of the evidence in the written record.

Under the Act, a city's decision to deny an application for renewal has to be based on an adverse finding with regard to one of the following:
(A) the operator's compliance with the material terms of the existing franchise and/or applicable law;
(B) the quality of an operator's service, including signal quality, response to consumer complaints, and billing practices;
(C) the operator's financial, legal, and technical ability to provide the services, facilities, and equipment set forth in the proposal; and
(D) the reasonableness of an operator's proposal in meeting cable-related community needs and interests, given the cost of meeting such needs and interests.

In this regard, the Cable Act has worked well to protect the interests of cities, consumers, and cable operators alike. Section 626(c)1(A) in particular, which allows cities to judge cable companies on their compliance with the terms of existing franchises as well as existing law, already covers employment practices, consumer protection, subcriber privacy, obscene programming, and other policy concerns. Indeed, since 1984, there have been only half a dozen contested renewal proceedings which went to court.

I am not aware of any evidence which suggests that the character of cable operators is a concern, or that it needs to be addressed in legislation. Allowing city councils to consider "ratemaking history" in the renewal process would only be a backdoor way of restoring the cities' ability to regulate cable rates--something which Congress rejected in 1984. The Cable Act has provided stability and due process for both cable companies and cities. I thus do not believe that Congress needs to or should amend the Act's franchising provisions.

2. If the Congress were to decide to reimpose regulations on cable rates, who do you believe should set the rates, the cities, the states, or the federal government?

As I have testified before your Committee, talk of rate reregulation is premature and will have a negative impact on the cable industry. However, if required to choose between city, state, or federal regulation, I would opt for control at the federal level.

Before 1984, when cities regulated rates, local politics, not economics determined the price of cable service. City councils had no coherent, long-term framework for making balanced decisions about cable rates or franchise conditions. Unlike state PUCs, which are governed by due process and have an appreciation for the need to balance consumer prices against the costs of capital investment and the right of utilities to earn a fair return on investment, city councils were driven by the political imperative of keeping rates down while increasing demands for special facilities, extra contributions to the city treasury, public works projects, and other concessions from cable operators. Rather than protect the consumer and guarantee reasonable service, city councils often made demands that cable operators could not meet or keep. As Dr. Malone emphasized to your Committee on November 16th, returning cable companies to the control of 10,000 different franchising authorities would Balkanize the industry, halt investment in programming, and undermine our ability to compete in both the domestic and international marketplace. Consequently, restoring city control over cable rates is the worst alternative of the three you posed.

Since 1984, when Congress freed cable operators from arbitrary city control, cable operators have been able to expand their investments in both programming and equipment as follows:

(1) Expenditures for basic cable programming jumped from approximately $300 million in 1984 to nearly $1 billion in 1989; this investment has led to a dramatic increase in both the availability and quality of basic cable program networks such as Nickelodeon, The Discovery Channel, Black Entertainment Network, ESPN, CNN, and C-SPAN.

(2) Overall spending by both basic cable networks and premium networks (like HBO, Showtime, and Disney) for programming has been stimulated by deregulation, almost doubling from $1 billion in 1984 to more than $2 billion in 1989. This spending has directly benefitted consumers by supporting a broad array of new and original programming on cable television.

(3) Deregulation has enabled operators to increase their investments in plant and equipment; spending for this purpose has increased from about $200 million in 1984 to over $500 million in 1989. These investments have benefitted consumers by increasing the number of channels available, and improving picture quality and reliability.

3. As you know, the study conducted by GAO found that the rates for basic cable service have increased an average of 29 percent from 1986 to 1989. What accounts for that increase?

There are two factors which contributed to the 29 percent rate increase noted by the GAO: (1) a post-deregulatory adjustment after 1986 for cable rates held artificially low since 1972, and (2) increased operating costs, particularly for programming. As I noted in section III(A) of my written testimony, average basic cable rates lagged 72 points behind the Consumer Price Index between 1972 and 1986. When rates were deregulated, many operators phased in rate increases in an attempt to "catch up" for the years that rates were kept artificially low. Even so, the average basic rate today is still $1.77 below what the 1972 basic rate would have been if it had simply kept pace with inflation: no attempt has been made to recover all lost revenues. Indeed, the GAO found that the average cost per channel remained at approximately 45 cents between 1986 and 1988.

4. You have indicated that the rate increases were accompanied by an increase in the program services provided. Have you considered giving subscribers the option of not receiving those new services and paying a lower rate?

The Cable Act provides cable operators with the flexibility to package programs and services as public demand warrants. Since implementation of the Act, most operators have streamlined their offerings and consolidated several tiers of programming, formerly available at extra cost, into one basic package. This simplification has met with wide customer acceptance, and the average basic service in the United States now provides many channels of diverse programming at one reasonable price (currently an average of 32 channels for approximately $14.77). Several companies, however, offer a "mini-basic" tier of services at a price lower than that charged for the broader package of programming which most consumers purchase.

There is also an economic reason for the consolidation of cable programming. Some basic services such as The Discovery Channel, Black Entertainment Television, The A&E Cable Network, and C-SPAN probably could not survive as stand-alone channels. It is the same reason why the Outlook, Style, and Sports sections of the Washington Post are all part of one newspaper: together, they form a viable package which can survive on subscriber and advertising revenues. Sold separately, the sections would probably fail.

5. In the Viacom suit against Time, Viacom contends that each cable operator is a monopolist in his own market and that access to pay cable programming is almost entirely controlled by the franchise holder in each market. Would you care to respond to that contention?

Viacom is making a specific complaint against Time, Inc. based on allegations of market-specific facts which may be the subject of litigation. In general, however, the video market, particularly for programming offered by the pay cable networks, is highly competitive and by no means controlled by MSOs. Indeed, the programming found on premium pay services is generally available from several different sources.

Cable TV carries three types of programming: (1) broadcast signals, (2) basic cable programming (e.g., ESPN, Nickelodeon, BET, The Discovery Channel, CNN, and C-SPAN), and (3) premium pay services, which primarily offer recent Hollywood movies. Most of the material seen on such premium pay services as HBO and Showtime is not controlled by cable systems nor is it initially available on these systems: Hollywood releases its movies first to theaters, then to videotape stores, and finally to cable companies. Movies have usually been available at a neighborhood theater or VCR store for six months before they can be seen on HBO or Showtime. Given that 66 percent of American households own VCRs,[1] and that there are more than 21,000 first-run movie theaters nationwide, pay cable programming is by no means "almost entirely controlled by the franchise holder in each market."

6. In the Viacom suit against Time, Viacom contends that each cable operator is a monopolist in his own market and that access to pay cable programming is almost entirely controlled by the franchise holder in each market. According to yesterday's Wall Street Journal, a settlement is in the works that could include an agreement to jointly operate a new comedy channel instead of each company starting a competing channel. At our June hearing, we heard testimony from Bob Wright of NBC that they had to commit in writing that they would not compete with CNN before they could obtain carriage on cable systems. It appears that there is a trend in the cable industry to discourage competition. Am I wrong?

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[1] A. C. Nielsen data as of July 1989.

There is no trend in the cable industry to discourage competition. To the contrary, cable television has increased choices for consumers by providing a sharp increase in the number of networks available. For example, prior to the advent of cable, there were only 3 national programming networks in the United States, all on broadcast television. Cable now provides 65 national and 38 regional networks, with another 29 in the planning stage.

Despite the rhetorical claims of some of our critics, MSO investment in programming--or vertical integration--has increased the breadth and depth of viewing choices available to consumers. In his study "The Competitive Consequences of Vertical Integration in the Cable Industry," which we submitted to the Committee in June, Dr. Benjamin Klein found that "cable operators are not using vertical integration to further any anticompetitive goals" (p. 2). He specifically noted that "...no individual vertically integrated MSO has the power to foreclose entry of competing cable programming networks" (p. 31) and that "vertical integration has not created a 'barrier to entry' into the cable programming industry" (p. 32). The result is that "cable consumers of vertically integrated MSOs have a wider selection of program choice among the most popular cable networks than consumers of nonvertically integrated cable systems" (p. 3).

Similarly, "vertically integrated MSOs are not using their ownership interests in cable programming as a tool to exclude competing delivery systems" (p. 3). Dr. Klein cites statistics which demonstrate that "home satellite dish owners currently have access to a wide selection of cable programming, directly from the satellite channel or from a number of competing third-party packagers, at attractive prices" (p. 4). Moreover, "most cable programming networks, including all of the top 10 and 22 of the top 28 basic and premium networks in terms of subscribership, currently are provided to MMDS systems" (ibid.). Dr. Klein concludes as follows: "Vertical integration benefits the viewing public by expanding programming availability while posing no current or likely future threat to competition" (ibid.).

With regard to Mr. Wright's complaint, his characterization of the facts may be highly subjective. It is not unreasonable to expect a new cable network to describe, in writing, what it proposes to offer in terms of format and how its offering is distinguishable from other networks already being carried by cable systems, e.g., CNN and FNN. It is well known in the television industry, as evidenced by the attached clipping from the January 16th issue of Cablevision, that as late as 13 weeks prior to the announced launch of CNBC, its management had not yet been able to articulate precisely what CNBC would offer. Under these circumstances, it should not have been surprising that some can generate enough local advertising revenue to cover the costs of paying for a network without separate subscriber fees; (b) have enough money left over to pay the operator for carriage on the leased access channel; and (c) still earn a profit.

8. In the study prepared for NCTA by Dr. Klein, there are charts demonstrating that since the Cable Act was passed there have been six new basic programming services that have made it to the top 20. All of these are affiliated with cable operators. No unaffiliated programmer has had this success. Doesn't this indicate the problem with unaffiliated programmers gaining access to cable systems?

Dr. Klein's study demonstrates the exact opposite: there is no evidence of a pattern of problems with unaffiliated programmers gaining access to cable systems. Moreover, as noted in response to question 9 below, many of the most popular cable networks are not owned by cable companies.

Dr. Klein found that "no MSO, either vertically integrated or not, possesses the economic power to exclude potential competitors from program supply" (p.3). Even TCI, which has interests in cable systems serving 23 percent of American cable subscribers, cannot control the programming on other systems, which reach 77 percent of the public (see p. 30). Moreover, Dr. Klein found that "there is no evidence that vertically integrated MSOs systematically exclude programming networks in which they do not have ownership interests. In fact, the four largest vertically integrated MSOs, TCI, ATC, Viacom and Cablevision Systems, are generally more likely than non-vertically integrated cable operators to carry the most popular cable networks in which they do not have an ownership interest" (p. 3; see also 28-48). If anyone could demonstrate that there was a problem with unaffiliated programmers gaining access to cable systems, it would probably be due to the fact that operators still have more incentive than anyone else to take the financial risks associated with new programming ventures.

9. Can you give us some examples of program services that are doing well, in the top 20 or 30, where there is no affiliation with a cable system?

Three of the top five basic networks have no connection with cable operators. They are ESPN, USA Network, and The Family Channel. These cable networks are owned by a broadcast company cable operators would have been reluctant to make a multi-year commitment to carry, and pay for, a new cable network--the nature of which remained something of a mystery.

In any event, CNBC was in fact launched on April 17th, 1989, and today, eight months later, is being carried by 875 cable systems serving 13.1 million households. As far as new cable networks go, CNBC has done rather nicely.

7. The Cable Act contains a provision providing for leased access to cable systems by programmers. I know of no instance of this provision being used. Why hasn't it been employed by programmers who want to get on cable systems?

Several factors have contributed to the fact that few programmers or businesses have made use of the commercial leased access channels mandated by the Cable Act. First and foremost, there has been little demand for these channels. When Congress enacted Section 612, it anticipated that leased access channels would be attractive to cable programming networks as well as Hollywood studios, independent producers, local programmers, and anyone else wishing to market video programming directly to a cable company's customers. I am aware of only a few instances in which anyone has sought to obtain a channel. The problem is not that leased access has been tried and failed; for the most part, it has never been tried. Although cable operators have made leased access channels available as required by law, we cannot dictate demand for those channels.

Second, as a general matter, cable programming networks--like broadcast networks--find that the local affiliate system is the most effective way to deliver their product. Cable operators, like local broadcasters, obviate the need for a programming network to establish a marketing infrastructure in each community where it seeks to distribute its product. The local affiliate model, for example, allows TBS to run its cable networks in thousands of communities across the country from Atlanta in much the same way that ABC, CBS, and NBC control their networks from New York. Unless the projected revenues from carriage on leased access channels sufficiently surpass the cost of establishing a presence in a specific local market, there remains more incentive for program networks to pursue affiliate agreements with local cable operators than to use those commercial channels.

Finally, it is important to remember that cable operators pay the programming networks for carriage of basic services, not vice versa. The economics of a leased access arrangement would stand this relationship on its head. Such economics would be very uncertain and do not guarantee that (a) an independent programmer

(CapCities/ABC) and R.J.R. Nabisco, two movie studios (MCA and Paramount), and the Christian Broadcasting Network, respectively. Other significant basic channels which do not have MSO affiliations are Financial News Network and The Nashville Network. In addition, one of the most popular pay cable channels, The Disney Channel, is owned by a movie studio, Disney, not an MSO.

10. As you know, to promote diversity, we have capped ownership of over-the-air television stations at 12. Why shouldn't similar limitations be placed on cable systems?

The Federal Communications Commission has promulgated a 12-12-12 ownership rule which limits any one individual to 12 television, 12 FM, and 12 AM stations, with the proviso that the 12 television stations may not reach more than 25 percent of the national audience (30 percent if minority-owned). To date, Congress has not established ownership limits for any communications industry other than to limit foreign ownership of broadcast, common carrier, and aeronautical radio properties to 20 percent.

With regard to ownership of cable systems, the cable industry is not highly concentrated as measured by either the top four firm concentration ratio or the Herfindahl-Hirschman Index (HHI). A market is considered concentrated when one firm, or a small group of firms, has a sufficient share of the market to exercise power over it. The Department of Justice, and prevailing economic theory, consider this market power to exist when the four firm concentration ratio reaches 50%, or when the HHI reaches 1,000.[2]

Current data on the market share of the cable operators that own a multiple number of local cable systems (MSOs) show low levels of concentration. Applying the HHI index to the top 20 cable MSOs, the resulting HHI value of 467 falls well below the Justice

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[2] U.S. Department of Justice Merger Guidelines, p. 18. Note that the HHI threshold of 1,000 is a minimum level of concentration. The maximum HHI level attainable is 10,000, which represents a pure monopoly situation (one firm with 100 percent of the market = 100 x 100).

Department's threshold of 1,000.[3] Thus, according to this measure of market consolidation, the cable industry is not highly concentrated.

Using the four firm concentration ratio, the conclusion is the same. According to the most recent data available, the top four cable MSOs have attained a 35 percent share of the cable market, a share far lower than the 50 percent threshold that defines a concentrated market.

11. During the hearing we held on must carry last month, we heard testimony that some cable systems have a policy of never permitting carriage of low power television licensees, even where there is no other local broadcast service in a community. Is that true?

Cable system operators generally carry all local full-power broadcast television stations that would have been entitled to mandatory carriage under the FCC's most recent set of must carry rules, even in the absence of such rules. In addition, some cable operators do carry low-power television stations, although these stations were not entitled to carriage under either set of the Federal Communications Commission's must carry rules. Note also that low power television stations are specifically exempted from the public interest obligations which the FCC imposes on full-service broadcast licensees.

A cable operator's decision to carry low-power television stations is based primarily on the value of a station's programming and the availability of channel space on the cable system. (It should be noted that many low power television stations are simply passive translators repeating signals from distant broadcast stations.) I am not aware of any cable system operators who have a policy of never permitting carriage of low-power television stations.

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[3] In its guidelines, the DOJ states that although it is desirable to include all market firms, small fringe firms do not affect the HHI significantly and are therefore not critical. Only the Top 20 MSOs were used here because beyond the 20 largest MSOs, each smaller MSO captures less than one percent of the market, and thus the square of a number less than one will have little impact on the value of the index. The top 20 MSOs serve approximately 33 million subscribers, or about 65 percent of the nation's subscribers.

12. The home satellite dish owners and "wireless cable" operators assert that they are denied programming or are charged more for programming than the large, vertically integrated cable operators. Thus, potential competitors, who are often have the least financial resources, are placed at a competitive disadvantage. Is it in the public interest to permit this to continue?

The assertion by home satellite dish owners and wireless cable operators that they are denied programming is incorrect. As Dr. Klein observed, there is clear evidence that MSOs do not arbitrarily withhold programming in which they have a financial interest from competing distribution systems. Indeed, MSOs "see MMDS systems as another outlet for their programming product" (p. 55). All of the top 10, and 22 of the 28 most popular basic and premium networks, are sold to MMDS systems, including ESPN, Superstation TBS, HBO, CNN, Nickelodeon, Lifetime, and MTV.

As the attached paper on "Facts Concerning the Status of the Home Satellite Dish Industry and Scrambled Programming" shows, cable programming is available to satellite dish owners through a growing number of program packagers, as well as on an a-la-carte basis. (There are also over 75 unscrambled services available to home satellite dish owners free-of-charge[4].) In addition, cable programming is available to third-party packagers such as the National Rural Telecommunications Cooperative, Consumer Satellite Systems, The Satellite Source, Programmer's Warehouse, and American Programming Services. Finally, cable programming is available to others at reasonable cost, with the home satellite dish subscriber often paying less than the average cable customer for the same services. For example, Viacom's Showtime and 16 basic services are available to dish owners for $20.95 per month--$18.75 if paid annually--while an equivalent package costs cable subscribers $24.71 a month. Dish sales have risen in both 1988 and 1989, which indicates that the market is working and that customers are finding good value in the programming available through home satellite dishes.

A key policy question for Congress in this matter is whether owners of intellectual property such as cable programmers should continue to have exclusive rights to the distribution of their products. The FCC recently reaffirmed the exclusivity rights of broadcasters in its syndex proceeding, and Congress underscored the exclusive distribution rights of cable programmers and broadcasters in the Satellite Home Viewer Copyright Act of 1988. I am not aware of any compelling reason for changing the principles of exclusivity which underlie our nation's copyright laws. In the absence of any such need, cable programmers should continue to have the right to distribute and market their product as economic and policy conditions warrant. They certainly should not be singled out for unusual treatment, just because their product happens to be distributed by cable or satellite, anymore than movie studios should be discriminated against, just because they sell theatrical distribution rights only to selected movie theaters.

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[4] Satellite Broadcasting and Communications Association, Satellite TV: Facts at a Glance, September 1989, p. 1.

However, the debate over program distribution and volume discounts is not just about access: it is about who gets to keep the additional margin available from distribution businesses that have lower capital and operating costs. Even if one believes that there is a legitimate problem with distribution, the object should not be to mandate a uniform wholesale price, since that would merely give the additional margin to the alternative distributor for efficiencies developed over time, and at considerable expense, by the cable operator/programmer. Rather, the object would be to ensure that the alternative distributor gets a wholesale price which allows him to compete fairly with the cable distributor at the retail level. This already occurs, as I noted above in the comparison between what home dish owners and cable subscribers pay for similar programming.

Senator INOUYE. Thank you.

I will call next on Mr. Malone.

STATEMENT OF JOHN MALONE, CHAIRMAN, TELECOMMUNICATIONS INC.

Mr. MALONE. Yes, sir. I guess it is mornings like this that I wish I had studied public speaking instead of thermodynamics in school.

I believe that the Cable Act by and large has been a big success. When back some years ago, Congressman Wirth, now Senator Wirth, told a group that I was with that we would ultimately be judged by the quality and diversity of the programming that we could bring to the American public, I think in that regard, the industry has been very, very successful.

We now have over 120 national and regional cable networks expanding viewing diversity, and there are 30 more projects currently, I understand, in development.

United States television is now the envy of the world. We are exporting our programming throughout Europe and Asia. American cable companies are constructing systems by invitation in Europe and participating in the construction of cable systems in Asia—all driven by the intellectual property of U.S. programming.

I do not believe any longer can television in the United States be regarded as the "great wasteland" that it was 10 or 15 years ago.

The question is at what cost has this been wrought.

Well, deregulation brought about a change in the structure of the cable industry. Many of you are familiar with the broadcast model of programming distribution in economics, where the networks, in effect, pay the local affiliate to distribute network programming.

The model in cable is quite the reverse. Cable companies pay, and pay very substantially, for the right to carry cable networks.

I don't want to repeat what Jim said except that it is on my list.

So, actually, the GAO report indicated that the cost per channel of cable has gone down since deregulation in real terms and has stayed flat in inflationary terms.

Overall, our tracking surveys—and, believe me, we are in the consumer marketing business with our products, so we survey our customers constantly—are very happy with the programming. Eighty percent are very happy or happy with the price/programming relationship.

Furthermore, as further proof in our market economy that our product is successful, the penetration of CATV has actually been accelerating, rather than decelerating, as the industry matures. That is, our product/price relationships would seem to be more appealing on the margin to consumers than they used to be.

Are our prices too high?

Well, the cable TV industry has the lowest return on invested capital of any media or communications industry.

A few years ago, we had some of the largest industrial companies in America in the business: General Electric, Westinghouse, American Express, Capital Cities.

They all exited the industry over the last five or six years, and all of them cited low return on investment, below their corporate objectives, as their reason to exit.

The only published statistics I was able to find recently comparing that return on invested capital are from a communications industry report, which indicated that regulated local telephone companies had a return on invested capital—this is pretax profits divided by average assets—of 14.9 percent.

The broadcasting industry, radio and television, had a return of 10.9 percent, and the cable industry had a return of 7.3 percent.

In effect, the entire industry would be better off investing its capital in government bonds than operating the cable business.

I might say in the case of our own company, we've been in business for 20 years as a public company. We have never paid a cash dividend to our shareholders. We've invested every dollar that we've been able to scrape together through equity sales or borrowings back into the cable business.

Our cumulative retained earnings over those 20 years is zero. We have plowed everything back into growth and renewing our technology.

Cable companies are cash alligators. They are capital alligators.

Our technology is evolving so rapidly that we cannot wait the 15 year franchise renewal cycle in order to provide good service.

We have to constantly reinvest, upgrade, expand channel capacity, and it is a process that consumer and has consumed much of our energy.

If anything, we probably have been too oriented that way and not given enough attention to customer service issues along the way.

We hope we can solve that.

I know that Senator Gore has referred to me in public as "Darth Vader," a cause of great humor, I guess, to a lot of my friends and employees.

My wife told me the other day that she found me to be more like the "Wizard of Oz,"credited with a lot more power and influence than I really wield.

Be that as it may—and I think our importance, TCI's importance and power is greatly overstated—whatever power we have we believe we have used rationally, intelligently, and sensibly.

Since deregulation, TCI has continued its pattern, which has made its prices the lowest in the cable industry. I think we are 47th out of 50th in a recent study in terms of average charges.

We have instructed our field people, who determine such issues as rates and services, not to raise their rates and prices each year since deregulation any more than the CPI plus the degree to which direct programming cost has exceeded the CPI.

So, in effect, most of our rate increases in TCI have reflected direct programming cost increases.

We have typically added two to three cable networks each year, for which the statistics give us very little credit.

I might say, with respect to investments in programming, that they are, in our company, very, very modest. They have always been motivated by a desire to create or help support niche businesses, which our surveys indicated our subscribers wanted and desired.

Such investments have been minority investments, such as in black entertainment television, funding C-Span, the Discovery Channel, the Vision Interfaith Network, and things of that nature.

I am very proud myself to be the first Chairman and a founding member of the Cable Television Laboratories, our industry's first combined effort at research and development.

We expect great things from that effort.

I might say in programming, also, we have invested from time to time to insure independence and continuity of supply. In that regard, we did lead. I played junior investment banker and led an industry effort to raise capital to keep Ted Turner in business and from having to liquidate his company a couple of years ago.

We have no control. We took low voting stock. Ted retains total control of the business, and we think that was pro-competitive and positive for the industry.

We have done similar investing in regional sports in order to try to change the format with which regional sports is offered to the public.

We believe that services such as regional sport should be offered on an optional-to-the-consumer basis, rather than mandatory. We do not believe that those services should be cross-subsidized by every subscriber because doing so essentially opens our subscriber's pocketbook to entrepreneur speculators and sports owners.

We think that is the wrong model for the cable industry, and that is why we are in that business.

I might say, finally, that we invest everything we've got and have invested everything we've got, including half of my deferred salary, in the cable TV business.

We believe in it. We believe in its technology. We believe in its promise for the future.

If there have been abuses, we certainly want to work with this Committee, with the government, with the regulators, in curing those.

Finally, our view of the Cable Act is that it did not deregulate the cable companies. What it did was transfer regulation in some aspects from the local governments to the Federal Communications Commission.

We fully expect that we are regulated. The form of that regulation is yet to be fully worked out.

Thank you very much, Mr. Chairman.

[The statement and questions and answers follow:]

STATEMENT OF JOHN MALONE

PRESIDENT AND CHIEF EXECUTIVE OFFICER, TELE-COMMUNICATIONS, INC.

Mr. Chairman and Members of the Committee, my name is John Malone, President and Chief Executive Officer of Tele-Communications, Inc. ("TCI"), an operator of cable systems throughout the United States. Thank you for the invitation to appear as a witness at your hearing to review the Cable Communications Policy Act of 1984.

This hearing, the one at which I testified in June, and similar proceedings in other Senate Committees and the House will likely only be part of a series of increasingly contentious and critical hearings on telecommunications issues generally. Although passions may well run high today and tomorrow, I believe that the most emotional, complex and important telecommunications issues this Committee will have to face are all still on the horizon, and in many cases have not yet even been framed.

A number of very intuitive observers, including you and other Members of this Committee, Mr. Chairman, have observed that we are now perched on the edge of a global telecommunications revolution. Enormous technological and economic forces have been set in motion which already have had dramatic consequences in the United States and foreign countries.

In commentary last week, the Cable News Network made a convincing case that the availability of Western television has dramatically accelerated political, economic and social change in the Soviet Union and Eastern Europe. Similarly, Time-Warner identified the economic power that will be unleashed in Western Europe in 1992 when barriers are removed in the EEC and Japanese incursions into U.S. communications industries as reasons for approving their recent merger, notwithstanding the increased concentration in our own domestic video distribution businesses that resulted.

The scale of the global competition likely to be faced by U.S. firms in the coming decade is well illustrated by considering a single Japanese firm -- Sony. Long a premier consumer electronics manufacturer, Sony is a leading manufacturer of televisions, VCRs, compact disc players and satellite receivers. It is also at the forefront of efforts to develop HDTV technology. More recently, it has made significant efforts to secure English-language creative capabilities through its acquisitions of CBS Records and Columbia Pictures. Sony is clearly positioning itself to take on all comers in every aspect of the video marketplace; what we as a nation need to do is make sure that U.S. firms will be able to effectively compete in the ensuing struggle.

With the increasing use of fiber optic, computer and satellite technology, the development of high definition television, continued geometric increases in the quality and variety of programming and the accelerating globalization of communications, it is a safe bet that video communications issues await your future consideration that will make those you have before you today seem less significant.

The Coming Video Communications Revolution

Nevertheless, this particular instance of legislative oversight is very important. Today, you continue the process of evaluating the very first tentative steps taken towards the video communications revolution that awaits us tomorrow.

Simply put, in the last ten years the United States has moved into a multichannel television environment. Consumers now demand a variety of programming that was unthinkable a few years ago and old delivery technologies are not adequate to meet this new demand. While cable, satellite, direct broadcast and microwave delivery systems are technologically capable of meeting the consumer's demand for more choices, to date cable has been the most economically feasible alternative.

This movement into multichannel video was entirely predictable -- in fact, many Members of this Committee accurately predicted it -- and the 10-year period over which it happened was a relatively long time, as I believe we will realize in years to come. Yet, even these first tentative steps have produced a great deal of controversy. Today and tomorrow, you again will hear from a wide range of interest groups who believe that the changes that have taken place have disadvantaged them. Cable is correctly identified as an agent of these changes and an aggressive supporter of more change. Consequently, cable is the target.

What this Committee and the Congress as a whole does in response to those complaints will have enormous implications for the role our nation will play in the coming video communications revolution. Your actions will have an effect on those of us who are preparing to compete against giant media companies abroad, and they will send important signals about our nation's resolve to our global competitors.

I am sure, Mr. Chairman, that you and the Members of the Committee have given a great deal of thought to the broader implications of these proceedings, and the proper role of government in overseeing the developments that are sure to come. This Subcommittee, Senator Gore's Subcommittee and others have held very interesting hearings on the subject in recent months. Nevertheless, please bear with me, as I offer some additional observations from one who deals with these issues daily from a businessman's perspective.

First, it is critical that we preserve as much of an unfettered market as possible in telecommunications. Aggressive municipal regulation of cable delayed the advent of multichannel television for at least ten years in the United States; in the rapidly-developing global environment, such delays in the future may prove the death knell for U.S. competitiveness.

Second, every suggested remedy for temporary inequities or imbalances in our telecommunications marketplace should be judged for its impact on America's effort to compete in the global video communications marketplace that is rapidly being created.

I am aware that all of you hear a lot about yesterday's problems, a little about today's and practically nothing about tomorrow's. Nevertheless, as many Senators here have said, it will be especially important to be forward looking in your efforts here, since short-term solutions are likely to work against the best interests of the American consumer.

Third, I do not believe it is possible, even if we wanted to, to return to a simpler age when the entire video marketplace was dominated by the three broadcast networks and over-the-air television generally. Obviously, broadcasters will always be very important, and those who make a special additional effort to program for cable and other media will prosper. However, those whose response to the video communications revolution is to ask government to freeze the status quo will be the early casualties of global competition.

Fourth, government clearly has a role in correcting temporary inequities that might arise, but it should do so only through targeted national regulation when the case for such regulation has been clearly made. Local regulation represents an anachronism; to retreat to a balkanized system of local regulation would permanently cripple any chance the cable industry would have to compete effectively in the global marketplace.

I suspect adopting the necessary long-term perspective is no easier for you than it is for us as business people. As elected officials, you are naturally responsive to the views of your constituents. In cable, I think this leads to a preoccupation with the retail side of our business. While this is certainly appropriate for customer service issues, on the more complicated questions, such as vertical and horizontal concentration and prices, the answers are likely to be found elsewhere. In our company, for example, all of our decisions regarding size and most of the important decisions about vertical investment are reactions to the realities of the program production and wholesale distribution network. I hope today to provide some focus on the economic forces shaping this marketplace.

The Cable Act Has Worked

You have gathered today to review a federal law passed only five years ago -- The Cable Communications Policy Act of 1984. I would like to review the Cable Act in the context of the principles that I have outlined above, and then comment specifically on a number of the issues that have been brought to your attention.

The Cable Act has helped America prepare for the video communications revolution. Freed from the artificial constraints of rate regulation, the industry has been able to attract the capital necessary to make needed investments to wire costly urban areas, to increase the number of channels offered, to improve the quality of the cable signal, and to upgrade the level of customer services.

TCI's own experience serves as a point of reference. TCI's capital costs in 1989 will be about $390 million. Since all but one of our new-builds are winding down, most of that money will be spent on rebuilding and replacing cable systems. During the five years from 1984 to 1989, TCI's total capital expenditures were about $1.2 billion. During that same five year period, we reported earnings of about $160 million. We do not regret these capital expenditures, for they have produced a better product for our subscribers and made us a stronger competitor.

In addition to improvements in technical quality, we have also focused on our dealings with consumers. TCI operations executives from throughout the country recently visited Washington to participate in the announcement of "The Customer 1st" program, a detailed 20-point national customer service program, which TCI will roll out company-wide in 1990. After extensive customer research and planning, we have identified the elements of this program, which include new, more efficient telephone systems, expanded office hours, employee training programs and service guarantees, as the best way to ensure our customers receive rapid and quality service.

Our systems now average about 36 channels. TCI is not alone in increasing channel capacity, and the availability of additional channels has fostered the development of more programming networks seeking to fill those channels. When the Cable Act was passed in 1984, there were 43 national satellite-delivered video cable services. Today, there are 65 such services already in operation. It seems that we hear new programming proposals virtually daily; nearly 30 more are in various stages of development. Innovative cable offerings such as CNN, Black Entertainment Television, Nickelodeon, Discovery Channel and C-Span have fundamentally changed the way American consumers think about video programming.

This programming, which offers the American consumer a range of video alternatives unknown in the rest of the world, is a critical development, since American programming sophistication is one great advantage the United States will carry into the global communications competition. In survey after survey, subscribers tell us that the diversity and variety of cable programming is the most important reason they subscribe to cable.

Contrary to popular opinion, however, the creative process of producing quality programming is both very expensive and very risky. Given this fact of life, TCI has tried to do what it could to encourage the creation of more and higher quality video programming choices to its subscribers, choices that are available today in significant part because of substantial investments by TCI and other cable operators.

The cost of such innovation and diversity has been high. Our 1989 programming expenditures increased 48 percent over the prior year. During the period 1985-1989, our expenditures for basic programming increased by over 248 percent. According to a leading industry analyst, the basic cable networks in aggregate will spend $935 million for programming in 1989, nearly triple the $340 million spent in 1984. When all forms of programming are taken into account, cable operators will likely spend in excess of $2.5 billion in 1989 for programming. The result is that cable subscribers are receiving a higher quality, more diverse product than ever before.

The Real Facts About Cable Prices

Thus, we have made great strides since the passage of the Cable Act, but at what cost? Has the virtual end of price regulation unleashed a monopolistic cable monster to prey on the cable consumer? This is what some would have you believe, but the story, like many political stories, bears little resemblance to the facts.

The fact is that, before the Cable Act, the industry was the prisoner of a highly politicized scheme of local regulation. The Cable Act was passed because everyone agreed the old scheme of local regulation was unworkable. Between 1976 and 1986, cable prices were allowed to increase at only two-thirds the rate of inflation; in some cases, dramatically less. Before the Act, the franchise process, particularly franchise renewals, was an uncharted minefield. No uniform guidelines existed from community to community. The franchising process was often used as a tool for accomplishing social or political goals. An incumbent operator had no assurance that upon franchise expiration its cable business would not abruptly cease even if it had provided outstanding service. The adverse incentives on continued investment are obvious.

While TCI did not for the most part join the franchise bidding wars of the 1970's, we still have experienced our share of regulatory horror stories:

- in one community where we started out with a $5.00 basic rate, we received only two rate increases totaling $1.50 in 16 years;
- in another community, our rates were frozen at $4.50 for 17 years;
- in another, we were required to subsidize the operation of a local non-profit charitable institution as a condition of our franchise; and
- in another, we were "requested" to help build a cultural center as part of our franchise renewal process.

Such regulatory disasters were long perceived in the capital markets as the major disincentive to the investment of the funds needed by the industry to realize the growth and development that everyone views a as an important public communications policy goal.

With the passage of the Cable Act, and the subsequent FCC determinations that effectively ended cable price regulation, artificially constrained prices did go up and, like the elimination of state price controls in Eastern Europe, this caused some initial dislocations. But as every study has shown, including the recently-completed GAO report, even the initial price increases that generated so much political rhetoric were very modest considering the history and increased costs of the industry. According to the GAO report, monthly subscriber bills increased an average of only 7 percent each year for the first two years after price deregulation. The revenue per channel remained essentially flat. This was a market adjusting to real competition for the first time.

Once that adjustment was made, you would expect a competitive market to do its own price regulation. Prices in a competitive market reflect demand for the product, the cost of producing the product, and the availability of substitutes. In a competitive market, price will be driven toward cost. This is exactly what has happened in the cable industry. Since the initial adjustment to deregulation, price increases on a monthly per subscriber basis have averaged slightly less than the rate of inflation. This graphically illustrates the highly competitive markets in which cable operates, since free market increases that do not match the rate of inflation mean either that the industry is not even recovering its costs or that it is becoming a more productive and efficient provider of services.

This recent price history is even more dramatic than it appears. The fact is that lower real prices today are buying a substantially enhanced package of cable services. Channel capacity has been significantly increased, rebuilds have improved the technical quality of the signals received, and many new cable programming services are available. It is clear that the true price of cable programming is decreasing, not increasing. This is why our viewers are increasing, and why we are gaining a larger share of the video audience: cable is selling a product people want at a price they think is good value.

Obviously, the cable industry's ability to price its product is constrained by the present and potential alternatives available to consumers. Indeed, the inability of other alternative video distribution technologies (other than video rentals) to gain significant market penetration is, in my view, primarily due to the fact that most cable operators have priced their service very competitively. Of course, we have some in our industry, as in any industry, who only have eyes for the short-term gain and are not interested in building long-term value. Unfortunately, this uncharacteristic handful provides the anecdotes that are used to malign the rest of the industry. The market will ultimately discipline these problems, but in the meantime they provide an excuse for those who want to attack cable.

TCI takes great pride in our competitive record; we are a vigorous price competitor. In fact, we rank 47th out of the top 50 MSOs in terms of revenue per subscriber. Today, we provide an average of 36 channels for approximately $15. This reflects both our competitive position and our significant productivity gains over the year. As a comparison, when I started in the cable industry twenty years ago, we generally offered 6 or 7 channels for $6, or $1 per channel. Since the rate of inflation during that time has been approximately 400 percent, if cable rates had simply kept pace with inflation the average cable bill today (for 6 or 7 channels) would be about $24, or $4 a channel. Instead, it averages about one-tenth that amount. This is a hard record to beat.

Since the passage of the Cable Act, our policy at TCI has been to try (to the extent competitive pressures permit) to adjust our prices annually to take account of inflation plus the amount by which programming costs exceed inflation. However, we are always looking for ways to price our product even more competitively. Today, I am pleased to announce a restructuring of our service which gives us the confidence to predict that we will be able to hold price increases for our basic, entry level service at no more than the rate of inflation, and hopefully even less.

The restructuring is based on the fact that under our contracts with most of our cable channels, we can reasonably expect that wholesale rates for these channels will not increase faster than expected inflation. Because some cable networks are incurring significant expenditures as they aggressively improve the quality of their programming, they cannot give us that assurance. Starting early next year, our plan is to offer subscribers the option of taking basic cable without these few networks and reducing their cable bill by an amount equivalent to our savings. Initially, the savings to those who take the basic service without optional channels will be from $.40 to $1.40 per month, depending on location. However, savings could be more in years beyond 1990, in part because of the increasingly competitive environment in which we operate.

Even ignoring for a moment the multitude of non-video providers of news, information and entertainment, three or more broadcast signals are currently available to 98 percent of cable's customers. Competition with other multichannel video providers is also getting stronger. Approximately 2.7 million home satellite dish owners currently enjoy nationwide access to cable programming. The wireless cable industry serves over 300,000 subscribers in major metropolitan markets and anticipates increased significant future growth. The FCC has authorized eight direct broadcast satellites that will offer multichannel programming directly to home viewers. Even though cable now passes 88 percent of all homes, it is only able to convince approximately 56 percent of those potential customers to subscribe to cable.

Moreover, as I noted earlier, existing competitors are not the only constraint on pricing in any market, including those in which cable competes. If an industry is performing at less than a competitive level, it will soon attract new entrants, lured by the prospect of earning the profits generated in such a situation. As such firms enter, over time they compete away any excess profit and return prices and profits to the competitive level, perhaps creating an even more difficult competitive environment -- more sellers competing for the same buyers. Therefore, if entry is a realistic possibility, present competitors have a significant incentive to perform as competitively as possible, in order to avoid attracting this new entry.

The flip side of such potential competition is that a new entrant cannot succeed unless it can offer consumers either a lower price or an improved product over present alternatives. The relative lack of success to date by alternative distribution technologies suggests that they have not yet been able to meet this basic market test.

Of course, they keep trying, and these efforts and the long-term threat these potential competitors represent are certainly one of the forces that influence pricing in the cable industry. Another is the threat of cable overbuilds, which have become a more common phenomena. Many cable overbuilds are nothing more than greenmail, but there are some successful overbuilds, and there is always the possibility that, if only one cable operator survives, it will be the overbuilder. Given this, and given the municipal support that often accompanies an overbuild, this threat has real competitive significance. Municipalities have the power and the ability to grant multiple franchises; they have historically not taken full advantage of that power, for various reasons, but it is a significant competitive tool if they choose to use it.

I believe that the best way to deter overbuilds is to provide a quality product at a good price. If there is no demand for a new entrant, there will be no new entrant. Unfortunately, even TCI hasn't always done a good enough job to discourage new entry, and we are competing today in a small number of overbuild situations. Where we are faced with new entry, we will vigorously compete. We firmly believe that we can succeed in this environment by providing a good product at a competitive price, and we are determined to do so.

Thus, it is clear to me that there are plenty of competitive forces already regulating cable prices, and that governmental regulation is both unnecessary and unwise. But if I'm wrong, the Cable Act already provides a mechanism for dealing with the problem by permitting rate regulation in the absence of "effective competition." The FCC is currently studying issues relating to rate regulation, including no doubt the present standard for determining what constitutes "effective competition." Any action in this area obviously should await the conclusion of the FCC's review and the publication of its October 1990 report.

There is a general point to be made here. There are lots of claims being made by cable's competitors. Most of these are nothing more than the complaints of the losers in the competitive race. The losers never admit they were slower;

instead, they were tripped or pushed or held. Claims are easy; supporting claims with facts is hard. There are very few facts being put on the table. The FCC is now gathering and analyzing the facts surrounding many of these claims. TCI pledges its full cooperation with that process. The time to discuss possible legislative changes is after the facts are gathered and analyzed, not before.

The Horizontal Concentration Myth

Price re-regulation is just one of the "solutions" that have been advanced to deal with alleged competitive problems. One of the most dramatic of the other proposals would place a percentage cap on the number of cable systems that could be owned by a single entity. Varients of this proposal would limit cable operator investments in programming networks.

It is hard to understand why this is even an issue, when there is no responsible case to be made that there is even a potential, much less an actual, problem. Even though national concentration statistics are not very meaningful for a local service business, if you look at national figures, the cable industry as a whole is remarkably unconcentrated.

TCI is proud to be the largest cable system operator. Yet of the approximately 50 million cable subscribers in the U.S. today, only 7.6 million are in systems in which TCI has a 50 percent or greater ownership interest. This represents about 15 percent of current cable subscribers. With respect to some of these subscribers, our discretion is limited by the fact that the companies are independently managed and by the legal concept of minority shareholders' rights. There are other companies and partnerships serving 3.6 million subscribers in which TCI has only an investment interest of less than 50 percent. In these instances, our control is even more limited since TCI itself is a minority shareholder.

Thus, even when viewed on a nationwide level, the current level of industry concentration is well below the minimum threshold established by the DOJ Merger Guidelines, which recognize an industry as "unconcentrated" when the concentration index is below 1000. Even if all of the subscribers in which TCI has any ownership interest were attributed to TCI, and we use the narrowest possible market definition (which is unlikely to be correct) -- retail sales by cable operators -- the index for the cable industry would be less than 800 and the four largest firms would serve only 42 percent of all subscribers. If a more realistic measure were used, considering only the subscribers in systems majority-owned by TCI, the index would be less than 500 and the four-firm ratio 35 percent. To put these concentration levels in some perspective, the concentration index for North American film distributors is over 1200 with a four-firm concentration ratio of 58 per cent. The broadcast industry is even more concentrated, since it is dominated by the three (and only recently four) networks. The cable industry is unconcentrated by either absolute or relative standards.

Of course, there has been some consolidation in the cable industry in recent years, but this has been dictated by the larger environment in which cable competes. The media business is driven by the fact that it costs a great deal of money to create the first copy of any media product, be it software, information or entertainment. Once you have created that product, however, the marginal costs of replicating and distributing it is very, very low. It is this simple fact that drives all media companies toward becoming very large -- the ability to spread their "first copy costs" over larger and larger number of consumers. The same economics drive a company towards increased size, whether is is a broadcast network, a cable programmer or a Hollywood studio. As the cable industry has matured, it has exhibited this growth and achieved those economies of scale.

The efficiencies associated with the increased size of cable companies have produced cost savings and contributed to the rate stability enjoyed by cable consumers in recent years. Recognizing these efficiencies, a number of small cable operators in the Midwest have banded together in a cooperative to try to gain some of the same economies of scale in their joint purchase of cable programming. The cooperative has enjoyed success with some programmers, but not with others. I fully support their efforts, and I see no reason why all programmers should not accord the cooperative and others like it the benefits of whatever scale economies they can offer.

The consolidation that has occurred in the cable industry is a natural progression of a maturing industry. It is also a natural defense mechanism for an industry whose chief suppliers (the movie studios) and primary competitors (the broadcast networks) are few in number and very concentrated. It is not a problem, competitive or otherwise. If it ever becomes a problem, the antitrust laws are available for use by enforcement agencies _and_ private parties, and the FCC is certainly capable of sounding the alarm.

The Vertical Integration Myth

Concerns have also been voiced about increasing vertical ties within the industry, particularly the investments in cable programming by cable system operators. These must also be put into perspective. Programming is likely to be America's greatest strength as we approach the video communications revolution. Since the current success of our programming efforts is due in no small part to the investments of cable operators, you should ask whether it is wise to shut off an important source of developmental funding at this point.

Some critics attempt to portray the cable industry as a many-headed hydra, linked by various forms of vertical integration, but this monster again simply does not exist. As a recent study established, many of the most important cable networks have no ownership ties at all with the cable industry. Three of the five top basic networks (ESPN, USA Network and The Family Channel) have no cable operator connection. Indeed, ESPN, the most widely viewed basic service which serves almost every cable household, is principally owned by one of cable's major competitors -- ABC/Capital Cities. USA Network is owned by two movie studios, Paramount and MCA.

As importantly, the nature of the links that do exist between programmers and cable operators varies considerably. Some services, like HBO, are entirely owned by the parent company of a a single cable MSO. Others, including the remaining two among the top five basic networks -- CNN and Superstation TBS -- have a large number of cable operators who participate in their ownership through very small individual interests.

The fact is that the success of cable has greatly expanded the market for programming suppliers, and the success of cable is inextricably linked to the creation of more and better programming. With an average of more than 30 channels available to subscribers, the cable industry has actually added opportunities for access to the creative community. Before cable, if a creative artist could not sell his product to the movie vendors or the broadcast networks, he or she did not get on the air. Twenty-four hours a day of cable programming requires an enormous amount of product. The explosion of cable networks has been a tremendous boon to independent producers and distributors. In turn, high quality programming gives us additional competitive tools. We see ourselves as a purchasing agent for our subscribers; if we do a good job, we will keep our present subscribers and add new ones. Programming investments are one way of doing that job well.

There is, contrary to some claims, absolutely no evidence that programming investments have significantly influenced carriage or channel alignment decisions. To do so would make no sense from a business perspective. In negotiating for carriage and rates for cable services, our objective must be to satisfy our customers. Their demand for particular programming, not our ownership interest, must dictate the carriage decision. The recent study by Dr. Benjamin Klein of UCLA shows this clearly.

Dr. Klein looked closely at the actual experience of cable programming, affiliated and unaffiliated. He concluded that there was no evidence that vertically integrated operators systematically exclude programming networks in which they do not have ownership interests. In addition, he found that vertically integrated operators were only three percent more likely to carry their own programming networks. His conclusion: "The net economic benefit of vertical integration in the cable industry is positive. Vertical integration benefits the viewing public by expanding programming availability while posing no current or likely future threat to competition."

Of course, since Dr. Klein's study was commissioned by NCTA, cable's critics instantly dismissed its conclusions as biased. But this resort to labelling won't work anymore; the facts are on the table. If someone wants to argue with those facts, let's see some new or different facts. The Klein study is the only study that deals with this issue systematically, not by anecdote. Those who would draw different conclusions have the burden of supporting those conclusions with facts.

TCI's experience in the programming area is probably typical. We never intended to become a cable programmer. TCI's primary business is as a cable operator, and we intend to retain this focus. TCI has made selective minority investments in programming in order to facilitate its role as a purchasing agent for its subscribers. We have been a defensive investor, not an offensive one.

These investments reflect two basic business goals. First, we continue to look for attractive niche programming that cannot be financed conventionally, even though it serves an important public policy interest. Our minority investments in Black Entertainment Television and the Discovery Channel, and our affiliation agreements with C-Span and the Vision Interfaith Satellite Network ("VISN") fall within this category.

Second, TCI believes it is important to maintain the independence of popular cable programmers where that independence is threatened because the programmer finds itself in financial difficulty. We and other cable operators made such an investment in Turner Broadcasting two years ago when Ted found himself financially overextended. Our minority investment not only maintained the independence of Turner

Broadcasting, it provided the financial stability that made possible the recent successful launch of Turner Network Television ("TNT"), which has been enthusiastically received by cable viewers.

Similarly, because of competitive factors in the premium programming tier, concerns have been expressed about the long-term viability of Showtime. To ensure the continued existence of a viable alternative source of premium movie programming, we recently announced that TCI would make a $225 million investment in Showtime to underwrite its continuing efforts.

The Sports Migration Myth

TCI has made substantial investments in regional sports programming. Not all of our cable subscribers are sports fans and not all are willing to pay higher cable rates for excessive sports rights contracts. The regional sports channel in which we have invested attempt to deal with this problem by "unbundling" the sports programming and making it available on an optional basis.

The amount of political heat generated by the recent Madison Square Garden/Cablevision controversy convinced us of the strong feelings this issue generates and of its importance to our subscribers. We hope that our support of regional sports programming, available on an optional basis, will fuel consumer demand for the full range of sporting events, not just traditional professional sports, and thus create a fully competitive environment that will prevent such episodes from arising in the future.

I know there is substantial concern in Congress and elsewhere about the potential migration of sports programming from broadcast television to cable. In my view, major sporting events such as the World Series and the Super Bowl will always be available on broadcast television, and I would strongly oppose any attempts to make them available exclusively on cable.

Cable's role should be to add to the number of professional games available on television, to provide more in-depth coverage of a particular sport, or to provide coverage of less popular sports that cannot command the advertising revenue to be viable on broadcast television. In the process, cable will increase, not decrease, the total amount of sports coverage available to consumers.

The early returns indicate that we have been successful in accomplishing these goals. A recent NCTA study of Major League Baseball ("MLB") concluded cable's regional coverage of MLB has served to supplement rather than reduce the number of games aired by local broadcasters. Similarly, a recent study of Prime Sports Network (a regional sports network partially owned by TCI) was undertaken in four geographic areas to determine its impact on the level of sports programming available to consumers. The study showed that cable has been responsible for a significant increase in the amount of sports programming available on both over-the-air stations and cable systems. In the period since Prime began operations, broadcast sports coverage increased by 15 percent and overall sports coverage increased by 55 percent in the four markets studies. The range of sporting activities covered was expanded, as cable offered a new events and activities such as gymnastics, Rugby, lacrosse, and even AKA dog shows, and also extended the type of coverage to include regional college football, NHL hockey, women's sports, high school events, and even delayed replays of professional games.

The Programming Access Myth

Concerns with access are widely overblown. A wide variety of programming currently is available to all distribution technologies, and this can only increase as channel capacity constraints force individual cable systems to make tough programming choices. Attractive programming that a cable system chooses not to carry will find coverage elsewhere, and the consumer will be the ultimate judge of who made the right decision. While those looking for a free ride or lacking the qualifications that a sound businessman requires in his customers will continue to have difficulty in obtaining programming, this is what would be expected in any competitive marketplace.

The facts show that responsible distributors of all types have been able to obtain the rights to carry virtually all programming when they are willing to pay the market price for such programming. This is demonstrated most graphically by considering the home satellite dish industry ("HSD"). This business has emerged from a somewhat turbulent infancy, caused in part by the need to establish a secure encryption technology and marketing apparatus to serve an unanticipated consumer demand. TCI, through its subsidiary Netlink, contributed to the process, by pioneering the concept of monthly program offerings and billing for HSD users and by offering an attractively priced retail package of broadcast and cable signals, at approximately two-thirds the price paid for basic service by our average subscriber.

The HSD industry is important, for it represents an attractive, efficient means of serving areas, such as rural communities, that cannot effectively be served by other video technologies. Policy makers should be concerned that their rural dish owner constituents be treated fairly. But the facts are clear: dish owners now have ready access to over 70 unscrambled signals at no cost and, through a number of packagers or directly from the programmer, to virtually every commercially available programming service at prices equal to or less than a cable subscriber pays. There are at least 20 companies marketing cable programming to TVRO owners nationwide, most of whom are not affiliated with cable operators.

As long as progress is made towards securing a consumer-friendly, secure encryption system, this will continue to be the case, for programmers will have the incentive to continue to create new programming, secure in the knowledge that they will be able to achieve a return on their investment. On the other hand, if signal piracy in the dish industry gets worse, TCI believes that overall programming availability will suffer, for no programmer can be expected to provide its product to a medium where it is regularly and systematically stolen.

Now, notwithstanding the fact that there is an extensive and attractive basket of basic and pay cable programming available to home dish owners and other delivery systems, we are told that some cable operators unfairly hold exclusive rights to popular programming, such as Sunday Night Football or TNT. This gives cable a competitive advantage, and some urge that exclusivity be prohibited.

The exclusive licensing of programming or other creative products is common throughout the entertainment business and is a well-accepted means of increasing the value of copyrighted artistic works. It provides a powerful incentive for distributors to create a demand for new programming.

Just as the success of "The Cosby Show" or "L.A. Law" reflects in part the efforts of NBC or that of "The Wonder Years" and "Thirtysomething" are partially due to the efforts of ABC, the cable industry can rightly claim some credit for the present success of much of the programming now shown on cable. Part of the reward for committing the resources necessary for this success is the right to enjoy the exclusive use of the programming. No one would give any credibility to claims that CBS could come in, once a show had become established on another broadcast network, and demand the right to carry it also. The case should be no different for cable.

Obviously, for the cable industry to credibly claim exclusivity rights, we must recognize these rights in others. TCI has vowed to do its best to comply with the FCC's new syndicated exclusivity rules that would achieve this result for broadcasters and it has not joined the court challenges to these rules. We are prepared to compete for programming, and we welcome any and all competition. What we are not prepared to do is to carry all of the risk of new and unproven programming, merely to see our competitors gain equal benefits if it is successful.

Other Broadcast Issues

Another source of recent complaints has been the "must carry" issue, but TCI's position is clear. We have long supported an industry-wide compromise on this issue and fully endorse the standard proposed by Senator Inouye.

As I have stated on other occasions, TCI has taken its cue on channel positioning from the FCC. Although our policy is flexible, we prefer, where technically possible, to carry local broadcasters on the channel assigned by the FCC. This allows a local broadcaster to promote his station throughout his market area using a common channel number for broadcast and cable.

This also removes any possibility that TCI can be accused of favoring another broadcaster or cable channel.

A similar approach has been adopted by most of the cable industry. According to a recent study, 94 percent of all broadcast signals are carried by cable on a channel equal to or lower than their over the air channel and 64 percent are carried on channel.

Nonetheless, a very small number of UHF independent stations have loudly demanded VHF carriage on cable despite their FCC-assigned UHF number. We are not aware of any right that a broadcaster has to be carried on a more favorable cable channel than the one assigned for over the air carriage. These complaining broadcasters also fail to recognize the substantial benefits of improved signal quality and broader carriage provided by cable.

Finally, most of the channel alignment complaints date from early 1987, when a large number of cable channels were added as a result of deregulation and both cable and broadcast channels were realigned on many cable systems. Such changes will probably be nothing more than isolated instances in the future. We are, of course, willing to work with the broadcast industry to resolve any remaining issues in this area and the FCC is available to deal with the issue, if necessary. As the channel capacity of cable systems in general increases, the problem will largely be solved of its own accord.

One other cable-broadcast issue that has attracted attention in recent weeks does not merit much discussion, but is, I think, worth mentioning solely because it clearly demonstrates the competitive motives that prompt many complaints. As part of its efforts to provide improved programming to its viewers, a cable system in Rochester, New York recently decided to program a single cable channel itself, using various syndicated offerings and local news features. Such efforts were strongly encouraged by the Cable Act as a way of improving the overall choice and quality of programs available to cable viewers. Notwithstanding this fact, the cable station's action has been strongly opposed by independent television stations, who have attacked the activity as anticompetitive and have gone so far as to request the FCC to initiate a rulemaking in this area.

What this opposition clearly reflects is the concern of local stations that they will face increased competition for viewers and advertisers. Such "competitive squeals" should not be given any serious consideration, particularly since it is clear that independent broadcast stations are continuing to enjoy substantial profits and revenues.

Cable-Telco Competition

Contrary to popular impression, telephone companies compete with cable today. Current law allows all telephone companies except for AT&T or the Regional Bell Operating Companies ("RBOCs") to provide cable service anywhere outside their telephone service areas or, with an FCC exemption, even inside their service areas. Moreover, there is a built-in exemption for phone companies to serve any uncabled rural areas within their service areas.

I do not believe telephone companies possess any economic or technological advantage as a video delivery mechanism. Because of the different demands placed on them, we are likely to continue to see at least two different delivery systems into the home. Any integration should occur at the home, not the system, level. To attempt to serve all communications needs through a single telephone wire would require massive subsidies by telephone ratepayers. This cross-subsidization is, I believe, inevitable, and thus I do not believe it is sensible to allow telephone companies to impose this indirect tax on their customers.

Conclusion

As this debate continues, we should not lose sight of the ultimate question: Has The Cable Act made American consumers better off? I think there can be no argument on this point; American consumers have more choices and at competitive prices that provide greater value than ever before. The Cable Act, and the resulting explosion of innovation, deserves much of the credit for this state of affairs.

Given this, any attempt to go back to the failed regulation of the past must overcome a heavy burden. Will such a step help American consumers or hurt them? Will such a step allow

American entrepreneurs to compete more or less effectively in the global marketplace? The public policy goal should be to encourage a system that permits and accommodates the enormous changes that are inevitable in this industry and ensure that that change works to the best interests of consumers.

Most of the complaints today are not from consumers. Consumers are voting with their dollars, and more and more of them are voting in favor of cable. If the ultimate consumer's needs are the touchstone of whether the Cable Act should be revisited, the answer is clearly "No." On the other hand, should this body, the FCC, the antitrust enforcement agencies keep asking tough questions and evaluating the performance of the video communications industry? Of course! Thus, I encourage your continued oversight and simply urge that any legislative initiatives be based on facts, not anecdote.

Thank you for the opportunity to appear today, and I will of course be happy to answer any questions.

MSOs are not using their ownership interests in cable programming networks as a tool to foreclose the market to competing delivery systems. Although exclusive licensing of programming is common in many parts of the entertainment business and is a well-accepted contractual element in increasing the value of copyrighted artistic works, vertically integrated MSOs are not demanding such exclusivity for their cable programming. The evidence is that cable programming networks, including those networks with affiliations to MSOs, have been made available to home satellite dish owners and MMDS systems.

5. Equal Treatment Under The Law

As a matter of policy, NCTA believes that cable programming networks deserve the same rights to enter exclusive distribution/affiliation agreements as are currently enjoyed by broadcast networks, motion picture distributors, and others engaged in the dissemination of intellectual property. As a matter of marketplace experience, cable network programming has not been withheld from consumers who choose a distribution technology other than cable.

VI. CONCLUSION

Mr. Chairman, the cable industry is realizing the promise of the Cable Act. In return for a fair and stable regulatory environment, the industry promised Congress that it would strengthen its services and increase the entertainment and information choices available to American television viewers. Some appearing before you during these hearings will suggest that the cable industry needs to be reregulated. Others will argue for "increased competition." Neither is warranted since we are currently regulated and already subject to competition. Moreover, that competition has been beneficial to American consumers and has provided them with a greater number of channels and a wider variety of programming than before passage of the Cable Act. We look forward to learning the FCC's recommendations regarding the Cable Act next year and will cooperate with members of this Committee in addressing any concerns that may arise.

ANSWERS TO QUESTIONS SUBMITTED TO JOHN MALONE

1. It has been suggested that the franchise renewal process needs to be revised to permit the franchising authority to take into consideration factors such as ratemaking history, employment practices, character qualifications, and ownership of other media interests. What is your opinion?

   The franchise renewal process of the Cable Act does not need to be revised.

   Moreover, a local government may simply grant a second franchise if an incumbent operator is performing poorly. Under the Cable Act local governments already retain substantial authority in this area. For example, a local government can deny renewal if an operator does not have adequate financial, legal or technical qualifications.

   Because of the continuing need to upgrade cable system plant to provide more programming choices and better service, as well as to keep abreast of the rapidly evolving technology, cable operators must have adequate assurances that they will be able to recover their capital investment. If cable operators are thrown back to the whim of local governments for renewal, the ability of the cable industry to continue to attract the financial capital necessary to meet the public's need for improved cable service could quickly evaporate.

   The notion that the return to a so-called "competitive" bidding process will result in increased consumer benefits is not a sound one. While we do not expect to be shielded from potential competition, Congress should not permit mayors and city councils to kick-out an incumbent operator solely because of the unproven and most always unrealistic promises made by a would-be operator seeking a franchise. In these circumstances, a prospective operator will be willing to make an uneconomic commitment solely to obtain a franchise. This would merely return the industry to the days of the bidding wars which we believe would substantially harm the industry and even more importantly cable subscribers.

2. You have indicated that the rate increases were accompanied by an increase in the program services provider. Have you considered giving subscribers the option of not receiving those new services and paying a lower rate?

   Yes. As indicated in my testimony, TCI agrees that it is important for both subscribers and the industry to have predictable and stable basic rates. That is the reason for our decision to remove from the basic tier those few services whose programming costs may continue to escalate beyond the rate of inflation so that the ever increasing cost of obtaining this programming will not continue to force basic rates even higher. Under our plan, only those subscribers willing to pay for those services which have continuing increased affiliation costs will be paying for these increased costs. Moreover, we are constantly surveying our customers to measure their satisfaction with our products and services. At TCI, we are particularly concerned over customer perceptions about the value of the cable services they receive. Out of the top 50 MSOs our basic service charges are 47th as measured in terms of revenue per household which, we believe, is the only objective method of measuring cable rates. Finally, it is also important to recognize that in addition to the practical constraint of how to sensibly market a multitude of programming options to subscribers, there exists very real technical limitations on the number and variety of programming options that we can provide currently. The industry's Cable Laboratories, of which I am Chairman, is hard at work on new technologies that we believe over time will result in allowing cable operators to offer more customer choice.

3. The Cable Act contains a provision providing for leased access to cable systems by programmers. I know of no instance of this provision being used. Why hasn't it been employed by programmers who want to get on cable systems?

   It is my understanding that there are a few cable systems that are providing programming on a leased access basis. The alleged failure of leased access to be more actively utilized, we believe, represents no failure at all, but is primarily the result of the success of the cable industry in meeting the diverse range of viewing needs. Under leased access, a programmer would pay a cable operator to obtain access to customers. Under the existing cable program affiliation arrangements, TCI pays substantial amounts of money to cable programmers to provide programming to our customers. Obviously, a programmer would prefer being paid to provide programming rather than the other way around. Where TCI makes a decision that our subscribers are not benefited by a provision of a particular program, and therefore declines to enter into an affiliation agreement obligating payment of subscription fees to a programmer, that programmer may seek access on our cable systems under the leased access provisions of the Cable Act. Consistent with the requirements of the Cable Act and channel availability we would certainly entertain these requests. Finally, it is important to bear in mind that only cable systems with 36 or more channels are subject to the Cable Act's leased access provisions.

4. Multichannel News, on April 3, 1989, reported that you are concerned about cable companies that do not have a real interest in program networks, and that you dread the thought of paying for cable programming and then seeing that money

leave the industry. That does not seem consistent with the idea that cable is dealing equitably with all interests. Would you care to comment?

To suggest that those comments somehow reveal an intent not to deal fairly with all interests is completely unfounded. My sole concern is that cable programmers reinvest profits to improve programming to cable subscribers, which is absolutely vital to the industry's long-term future. Our customers expect both operators and programmers to make the substantial investments necessary to improve both our products and services. My concern over the need of programmers to invest in the industry's future applies equally to all programmers, whether or not they are owned by a cable operator. TCI, for example, has historically agreed to increasing affiliation charges in response to commitments of programmers to invest in new program development. We will continue to do so. However, if those programmers decline to continue to invest in programming development, we would be less willing to pass along increased affiliation costs on to our subscribers, regardless of who owns the programmer. We are willing to ask our subscribers to pay more for programming only where programmers are willing to make a concomitant investment to the benefit of our subscribers by producing better programming.

5. During the hearing we held on must carry last month, we heard testimony that some cable systems have a policy of never permitting carriage of low power television licenses, even where there is no other local broadcast service in a community. Is this true?

We are not aware of any cable system that has such a policy. TCI does not. TCI has a policy of considering requests for carriage of low power television license stations on a case-by-case basis. We will consider carrying such stations where they would provide programming alternatives desired by our subscribers, where those alternatives are not otherwise available on the cable system, and where the service that must be deleted to make room for the LPTV station clearly has less subscriber appeal. We recently agreed to carry a Buffalo low power station for precisely these reasons.

Senator INOUYE. Thank you very much, Mr. Malone.

I will now call upon Mr. Robbins.

STATEMENT OF JAMES O. ROBBINS, PRESIDENT, COX CABLE COMMUNICATIONS

Mr. ROBBINS. Mr. Chairman, thank you very much for allowing me the opportunity to tell you who we are and how we have conducted our business at Cox Cable since the passage of the act.

We are not one of the largest cable companies in the Nation, but we are among the top ten. We have 113 franchises grouped in 24 systems in 17 States.

We have been in the cable television business for 27 years. Our parent company, Cox Enterprises, has been in the communications business for over 90 years, beginning in 1898, when James M. Cox bought "The Dayton Evening News."

Mr. Cox, elected Governor of Ohio in 1913, expanded into more newspapers, then into radio, and then, in 1948, the company ventured into television.

Entry into cable television came in the early 1960s, and was a natural extension of this entrepreneurial spirit.

I think it is clear from this history that we are a long-term player. Cox does not routinely buy and sell properties. We hold on to them. We grow them. We take our commitment to the communities and to our customers that we serve very seriously.

As a telling example, we invested $105 million in our system in New Orleans, a franchise that we won in 1980.

Tough economic conditions there have been as hard on us as on anybody else. Our operating losses in that system have totaled over $14 million. Yet, we have just made a major commitment to invest another $10 million in that system because it is the right thing to do for our customers there.

We operate our business with a long-term perspective and this attitude makes a tremendous difference in the way we do business.

I would like to share with you four ways that this attitude shows itself in action.

First, with respect to rates, any adjustments we make reflect inflationary increases in our operating costs, increases in costs for existing programming and costs associated with new programming and our need to receive a reasonable return on our invested capital.

For the years following passage of the Cable Act, the dollars that we have received from a customer household have increased, on an average, 3.75 percent per year, from 1984 to 1990. That was 3.75 percent. In the years, the CPI has increased an average of 3.6 percent. And yet, we have added scores of new programming to our systems.

We believe that this is a record of enormously responsible behavior.

Second, in the area of programming, we have added a significant amount of programming to make sure that our customers get the diversity and quality that they want.

Programming, as a percent of our cost of doing business, has risen from 21 percent in 1984, to a projected 33 percent in 1990.

In the last three years alone, our programming cost increases have been 20 percent in 1988; 9 percent in 1989; and 19 percent, we project, for 1990.

Our customers have demanded this new programming.

We will continue to explore investment opportunities like those we have already made in the Discovery Channel, Movietime, Viewers' Choice Pay-Per-View Network, to insure the continued diversity and quality of programming.

You should know that it has been the deregulation of rates which has allowed us to make these kinds of commitments.

Third, we are a leader in working out the nuts and bolts of good customer service.

To this end, last year we developed 21 hard, measurable standards in seven service categories, picture quality and reliability, phone answer time, front counter time, installation response time, repair response time, added value and courtesy to our customers, and marketing effectiveness.

These standards went on trial in all of our systems as of January 1, 1989, and as of January 1, 1990, our systems will be held accountable for each of these 21 separate service standards.

To make sure that we are serious about this, we have tied our managers' compensation into the improvement in customer service in their systems, as surveyed on an annual basis.

In order to help our employees meet these standards, we have invested millions of dollars in educating our front-line people, their supervisors, and our general managers in the how of providing good quality service.

Three thousand of our 3,500 employees are participating in a three-day, intensive training course, called "Focus on Added Value." In it, we teach our employees how to go about adding value to each and every customer interaction, how to make doing business with Cox Cable easy and enjoyable.

Fourth, we are deliberately and responsibly involved in the communities we serve. This community involvement ranges from providing senior citizens discounted rates in Cedar Rapids, Iowa; to working on a community project for a new library in Gainesville, Florida; to the development of a local, 24-hour news service in New Orleans in cooperation with the leading broadcast station there; to wiring the schools, high schools and elementary schools, in all of our service areas free of charge so that they can get assignment Discovery programming that has, we think, enormous potential for helping this country educate itself better.

I could go on and on and on with these kinds of examples.

My remarks, however, Mr. Chairman, would be incomplete without some acknowledgment of the problems in our industry. There are isolated instances of shoddy service, excessive rates, and trafficking in cable properties.

Speaking for my company, in particular, we don't like isolated incidents of this kind of behavior any more than you do because, typically, it is the bad news that makes the headlines.

As I have said, at Cox Cable we operate with a long-term mentality and we are clearly doing a great deal that is right.

Thirty-four of our franchises have come up for renewal since the Cable Act went into effect, and all 34 have been renewed. In addition, ten communities have awarded us brand new franchises.

I want to leave you this morning with the fact that no country in the world has the viewing choices that the American people have today, and at a price in our system that comes in at less than 14 cents per viewing hour for the average cable television household.

That world leadership position came about because you created an environment that allowed cable to be stable, creative, and productive when you passed the 1984 Act.

I ask you to remember the positive, effective job that the great bulk of the cable industry is doing before you give any consideration to changing the environment that has created this unique American success story.

Thank you, Mr. Chairman.

Senator INOUYE. Thank you very much, Mr. Robbins.

And now it is my pleasure to call upon the Chairman of the full Committee, Senator Hollings.

The CHAIRMAN. Now, you gentlemen have put your best foot forward, and it is very impressive.

On the other hand, you have a third of the Senate co-sponsoring numerous bills, half of this Committee. They see a problem, and finally, Mr. Robbins, you got to it: shabby service, excessive rates, and trafficking in franchises.

What do you expect? Having been a responsible participant not only in publishing papers and in broadcast but now in cable TV, what would you recommend that this Committee and this Congress do? Nothing?

You know that something is bound to come.

I figure from your experience you are pretty balanced.

If you were a Senator, what kind of control would you recommend to correct this trafficking in franchises, these excessive rates and shabby services? Would it be to do nothing, or just sit and fold your hands and hope? What?

Mr. ROBBINS. Senator, I guess I would say at the outset that, first of all, there is tremendous concern in the industry about the activity here in the Senate. I think you will find every cable operator that I know has this very much on his mind and is translating that into doing the kinds of things that we have been doing.

I would suggest that the rate deregulation portion of the act, which has really been in effect since the end of 1986, has only run for three years, and, really, I'm not sure that we have had a chance to show all of the things that we can do with respect to good service, with respect to providing the kind of proper price value that continues to have the American public buying into cable television.

So, I see what's happening in Congress today as a number of warnings, and I think that is very healthy for us in the industry.

I am not so sure that the time is right for any action because I think, as Senator Ford said, you will paint a number—and the majority of the industry who are doing the job right—you will paint them with a brush that the people who are not doing the job right deserve to be painted with.

The CHAIRMAN. If you had to have a modicum of reregulation, would it be at the city level, the Federal Communications Commission level, or where?

How would you approach it?

Mr. ROBBINS. Well, I would answer that by saying that I think any consideration of reregulation is very premature, and I think it would have a hugely negative impact on the industry. But if I had to choose, I would choose the Federal level.

The CHAIRMAN. The Federal level.

How about that, Mr. Malone?

Mr. MALONE. No question about it, Senator.

I think to turn regulation back to the local communities would be to "balkanize" the industry.

We have, as an industry, about 10,000 local franchises. To implement any change—let's say that the government wanted us to change our systems to accommodate a new standard for high definition. To comply, we would have to go back and get the approval of 10,000 administrative agencies. It is simply unworkable.

In order to add an additional channel that cost money, we would have to go back and get the approval of 10,000 administrative bodies.

Once again, it's simply unworkable.

I think that the model that the Cable Bill anticipated, which is that the FCC determines what is effective competition and where it is lacking, the worst case there is if there isn't effective competition in a market, regulation does go back to the local community, but with Federal guidelines and protections, which I think is perhaps ultimately the right model.

The CHAIRMAN. I heard you clearly on your poverty tale, that you are not making any money, that you can't give the poor stockholders a dividend, and that it's even worse than government bonds, and that anybody with any sense is getting out of it.

Your stock, when you started, if I had bought $5,000 worth of Malone stock when you started, how much would that be worth now?

Mr. MALONE. Quite a bit.

The CHAIRMAN. You're at least honest. You're not going broke.

How, on the matter of Senator Danforth's bill, as I understand it—I didn't know too much about it yesterday—the broadcasters are limited to 25 percent—you have the no limits. However, the broadcasters are in markets of five to ten competitors. The cable television operator is in a market with no competition.

I understand that Senator Danforth wants to pare that back down to 15 percent, and it's looking particularly at you, at TCI, I think it is. You are the biggest, the most powerful, the most monopolistic.

What about that limit?

You are doing fine. But we are not going to have a Malone there all the time who is fair and compassionate and investing, and everything else of that kind.

You might get a greedy politician all of a sudden taking over your business, and then we'd be in the soup.

What about that?

Mr. **Malone**. Well, first, as far as the appreciation of our stock, I think if you'd put a dollar in 20 years ago and had put it in Federal bonds, and then compounded it forward for 20 years, you would expect your stock to go up, too, or you would fire the management.

The appreciation of our stock, I think, is a direct result of the reinvestment of all of our capital and does not really represent any excess profitability.

The return on assets I think is the relevant figure there, in terms of the profitability of the industry at large.

With respect to TCI's size, we don't think it makes sense as a matter of national policy to chop up American companies into such small units that they become easy prey to either vertically integrating competitors or to foreign competition.

But that is a different issue.

As far as TCI is concerned—and I believe Senator Danforth's bill is now 15 percent, instead of 10 percent—it is clearly a TCI divestiture bill at that number because we are the only company with in excess of 15 percent market share.

Depending on how you define it, we could have somewhere between 16 percent and 22 percent of the market.

I think that it is a legitimate issue for the government and the regulators to look at issues of market power. I think it is a legitimate issue.

We always thought that that was the FCC's job.

We know that the FCC has all of the authority it needs to do virtually everything in the proposed legislation. So I guess we're a little unsure of the processes of government as to why that isn't adequate.

You know, we really are not bad guys. We really are not trying to build an empire. We really are willing to listen to the directions of government.

Every acquisition we've done, every investment in programming that we've done has been approved by the Federal Trade Commission, approved by the Justice Department.

On a number of occasions in the last five years, I personally and members of my staff have sought guidance from the Federal Communications Commission in terms of the appropriateness of the various things that we do and the way we look at how we should invest our shareholders' dollars.

Unfortunately, there has been an absence of dialogue in the past in this area.

You know, we would welcome a dialogue with government on these areas. We are firing blind here. We don't really know.

Now, my job is to do a good job for my shareholders, my subscribers, and my employees, and I try very hard to do that. But if we're doing it wrong, we need feedback.

It is a shame to have to come to Washington, D.C. and the Senate Commerce Committee to get feedback from the government in terms of if we are doing something wrong.

The **Chairman**. Thank you, Mr. Chairman.

Senator **Inouye**. Senator Packwood.

Senator **Packwood**. Mr. Malone, you made a statement and I didn't quite get the end of it. It was that cable systems pay and pay handsomely to carry, and then I didn't get what you said.

Mr. Malone. To carry the various cable networks.

Senator Packwood. Explain what you mean, please. You pay CNN to carry it?

Mr. Malone. Correct.

Senator Packwood. But you don't pay CBS to carry it?

Mr. Malone. Well, we don't pay CBS, but we do pay a compulsory license fee for the carriage of CBS. The money goes to the underlying programmers. It doesn't go to CBS, is my understanding.

So we pay everybody.

Senator Packwood. Do you mean that you pay a copyright fee?

Mr. Malone. Correct.

Senator Packwood. And it goes into that Copyright Fund and is distributed to the programmers?

Mr. Malone. Well, we really carry the local affiliate of CBS, and that fee essentially goes into, the Copyright fee goes in.

If we aren't able to pick up the local affiliate with an antenna, then we pay a satellite fee or a transportation fee to get that signal to our head-end.

So in those two ways, we even pay essentially the broadcasters for their services.

Senator Packwood. You pay the programmer, don't you?

Mr. Malone. No. We pay it into a tribunal, into the Copyright Royalty Tribunal.

Senator Packwood. Did you have a comment?

Mr. Mooney. Yes. I'd like to help out a little bit on that.

We don't really carry CBS. We carry the CBS affiliate. And, if I may anticipate what you're getting at with respect to payment for that, our attitude toward this is that Channel 9, for example, here, which is the CBS affiliate, is licensed to cover Washington.

I live in Washington. If, for some reason, I cannot get a clear picture from Channel 9 and want to pay somebody to provide me with an antenna service to help me receive that picture clearly and it is intended for my reception in the first place, we would think that transaction is between us and the guy who provides the antenna service, and it's no skin off CBS's nose that we should be purchasing that antenna service and the fellow who is selling the antenna service, in other words, the cable operator, makes some money.

Senator Packwood. You've lost me on this.

You're in Washington and you're not getting a clear signal from Channel 9.

Mr. Mooney. Right.

Senator Packwood. Now run this by me again about the antenna.

Mr. Mooney. When the cable operator retransmits the local signal of Channel 9, which carries the CBS fee, what the cable operator is doing is selling an antenna service to sharpen up the picture and the transmission for the benefit of the local viewer.

In that instance, when the local viewer is in the same market as is the broadcast licensee, Channel 9, we don't think that the broadcaster is losing anything or anything is being taken away from him by the fact of the antenna service being sold by the cable operator to that subscriber.

In other words, we don't think he has a claim to be compensated.

Senator PACKWOOD. So, in essence, what you are saying is if they don't want to run it through your wire and they want the viewer to have a clear picture, they ought to put up a more powerful transmitter——

Mr. MOONEY. That's one of the things I'm saying.

Senator PACKWOOD [continuing]. Or distribute it themselves over the air so that the customer can see it.

Mr. MOONEY. Yes.

In part, the cable retransmission makes up for some of the deficiencies of broadcast technology, including the ability to provide a clear picture throughout the area the licensee is supposed to be serving.

Now, if you had a different situation and the fellow who is running the antenna service had to pay Channel 9 for the privilege of doing that, I suppose you'd be converting CBS into pay television. It wouldn't be free anymore. The cable operator would merely be operating as a collection agent.

Senator PACKWOOD. I'm only recently a cable subscriber. I didn't used to live where there was any cable. And I realize that there are dozens of channels.

But in terms of what is watched on cable, how much of it is rebroadcast network and how much of it is non-network?

Mr. MOONEY. Let me put it this way. In pay cable homes, which is a figure I happen to have in my head, which are cable homes which take not only the basic service but also at least one of the premium movie services, the broadcast networks get a little bit less than 50 percent of prime time viewing. The remainder goes to the cable services and to independent stations.

Senator PACKWOOD. In your statement, you say NCTA agrees with this Committee's desire to reinstate must-carry.

Is that a new position?

Mr. MOONEY. No, sir.

We have taken that position for several years. We, in fact, reached a compromise with the broadcasters on must-carry in 1986, which we recommended to the FCC and which was ultimately adopted by the Commission, but subsequently overturned in the Court of Appeals for lack of an adequate record.

We have since that time openly, avowedly, and unashamedly expressed our willingness to agree again with the broadcasters, essentially on the same set of rules and recommend that they be enacted by the Congress this time.

But I think we have had a little problem. Broadcasters have had a little problem getting their hands around that one.

Senator PACKWOOD. Well, what is the problem? They say they want must-carry.

Mr. MOONEY. Yes.

Senator PACKWOOD. You say you want must-carry.

Are you talking the same thing?

Mr. MOONEY. Yes, I think we're talking about the same thing in terms of must-carry per se.

The broadcasters have added to the pot, however, the issue of channel positioning, where they essentially want the right to be frozen permanently wherever they happen to be located now. So if

Channel 32 were on Channel 5 on the cable system for historical reasons, they want the right to stay there forever.

Our position has been that if it's okay with the broadcaster and the cable operator that he should be there, the government shouldn't be interfering; but in the event of a dispute, they should have a legal right only to be in the position that the FCC gave them off-air.

That split has prevented the two industries from closing this up.

Now, the Chairman of the subcommittee a few weeks ago suggested that what we might do here is simply enact the must-carry provisions that everybody agrees on and let the FCC decide the channel positioning issue, and we've said that we'll live with that in an effort to get this thing behind us. But I gather that is unsatisfactory with the broadcasters.

Senator **Packwood**. Let me ask you a last question, and then my time will be up.

This concerns a Merrill Lynch statement about the value of the programming to you. This is their statement: "In our view, it is fair to say that the networks account for much of the value of the cable service for which subscribers now pay about $13 billion annually. It is clear cable operators and cable-originated program services are essentially subsidized by the broadcast networks and television stations. '

Is that an accurate statement?

Mr. **Mooney**. I don't think so.

I'm not familiar with that statement. But I don't think the cable programming services are in any way subsidized by the broadcasting industry.

In fact, we do a great deal of good for the broadcast signal, both in terms of its clarity and in terms of extending its reach.

It is for that reason that I think the broadcasters for so many years have been up here asking you to put into permanent law the must-carry requirements.

In the interest of making peace with them, we have been willing to concede that. But it seems that every time we get close to an agreement, the ante goes up a little bit. And now there seems even to be a segment of the broadcasting community that wants both must-carry and must-pay, which we think is overreaching just a bit.

Senator **Packwood**. Thank you, Mr. Chairman.

Senator **Inouye**. Thank you.

Senator Ford.

Senator **Ford**. Thank you, Mr. Chairman.

Mr. Mooney, you and Mr. Malone both referred to the GAO report and how good it was for you that the price had not gone up.

You referred to it because it was favorable. But tell us, really, how was that GAO report achieved? How did they get their information?

Mr. **Mooney**. The GAO sent out a questionnaire to a sample of cable systems throughout the country, which GAO selected with an eye toward statistical balance. They got what I understand was a 75 percent response rate which GAO described as quite high for that kind of thing, and assigned a 95 percent confidence rating to it.

I am not a statistician, Senator. But I understand from people I know who are statisticians that that kind of response rate is quite high.

Senator **Ford**. Well, Mr. Mooney, it was a purely voluntary thing.

Mr. **Mooney**. Yes.

Senator **Ford**. And GAO sampled 1,950 of 8,908 cable operators at the time, and they got 499 responses, which was 26 percent—that is, 26 percent failed to respond to the GAO.

Now, I wonder if among those who failed to respond would have been the cable system in Louisville, because their rate increase has gone up 204 percent since 1986.

Mr. **Mooney**. Senator, the only comment I can make on those cable systems which failed to respond is——

Senator **Ford**. That they are high percentage increase cable systems.

Mr. **Mooney**. No, sir. The only comment I can make is that in the data that the GAO supplied as part of its report, they seem to be mostly very small cable systems, and perhaps people who were simply unable to cope with the paperwork.

Senator **Ford**. They didn't audit any of them, did they?

Did they audit any of them?

Mr. **Mooney**. Yes, I believe they did.

Senator **Ford**. How many?

Mr. **Mooney**. I can't tell you off-hand.

Senator **Ford**. You know, I just don't believe they audited. They may have.

Mr. **Mooney**. Yes, I think they have.

Senator **Ford**. What—one or two?

Mr. **Mooney**. Oh, no, sir. More than that, I believe.

Senator **Ford**. Well, you just go down through the list: Ashland, 94 percent; Bowling Green, 123 percent; Hazard, 131 percent; Louisville, 204 percent; Madisonville, 95 percent.

Now that's my State. That's right in my back door.

And you come in here and tell us that it's an average of 20 percent or 26 percent. Why it's just not there when you get right down to it in my particular State.

Now how in the world can you take 1,950 and get 499 that fail to respond out of that, and those were voluntary responses, and I doubt seriously that there was an audit. There were very few audits.

Then we come in here and you're telling us that it's 95 percent accurate.

Mr. **Mooney**. Well, actually, I am reporting what the GAO said with respect to its own study. But I would add to that that the GAO figures do pretty much correspond with what other sources of data there are in this area.

Senator **Ford**. Well, I'm going to ask the Chairman if we could have the GAO come in and report because you all are saying this is the "Holy Grail," and I want to be sure that it is.

I want to find out how many and what size they were, that sort of thing, and who failed to respond.

If you look at my figures, Mr. Mooney, they don't jibe with GAO at all. And I'm sure out of those who failed to respond there are those who happen to have the 200 percent increases, in three years, by the way.

If you think the consumer is not feeling gouged in my part of the country, they are. And you know who owns the systems.

Mr. Malone, you said if we leave the FCC alone, it has the rules today to do whatever this legislation is asking to do.

Is that correct?

Mr. **Malone**. That's my understanding of it. Yes, sir.

Senator **Ford**. Well, who advised you of that? Your high-paid corporate lawyer, I guess?

Mr. **Malone**. Yes.

Senator **Ford**. Well, the FCC—you know, Dad always told me this: I'm not a lawyer. So he said get yourself a good lawyer and stick with him.

I think you ought to do that.

But the FCC rules that you are operating under, as I understand it, were developed for the broadcast community, and there have been no changes. And you are operating under rules that are for broadcast, and none basically apply to cable.

Is that correct?

Mr. **Malone**. I'm not sure exactly which of the rules you are referring to, sir.

Senator **Ford**. Well, all the rules—historically.

Mr. **Malone**. Well, programming rules, yes.

Mr. Mooney would have a better feeling for the law here than I.

Senator **Ford**. Well, you know, I worry about Mr. Mooney. If you had a tape recording of every appearance that he's made here, he made the same statement at this or other Committees, that we have problems, but we're trying to correct them, and if you'll just leave us alone and give us time, we'll get them done.

He's even wearing one of his less expensive suits today.

Mr. **Malone**. Let me try to respond to the best of my knowledge of what I understand to be the law here.

I understand that the FCC could adopt horizontal limitations.

Senator **Ford**. But they haven't yet.

Mr. **Malone**. But they haven't. They could. They have the power to do so.

They could adopt vertical limitations.

They could redefine effective competition and extend rate regulation to a larger number of communities than currently have the power to regulate.

That's my understanding.

And they could adopt another must-carry rule if they could make an adequate showing to keep it from being thrown out in the courts.

So, in all of those areas, I believe the FCC has the authority to act. At least that is what I've been told.

Senator **Ford**. Let me ask you this, Mr. Malone.

It seems that there have been enormous sales. Even in the little community where I live it's $24 million. That's big.

It seems to me like there has been three years of buying and selling and not much enlargement. I hear all of these figures from Mr. Robbins.

You know, I like what you say, Mr. Robbins. But I would like to investigate a little more and see if that is accurate all over the system. Apparently it is not because you said you still have pockets of problems—overzealous, higher prices, sloppy sales.

Mr. **Robbins**. I was referring to the industry when I said that.

Senator **Ford**. You mean that you're admitting that the industry is gouging the consumer and has sloppy service in some places?

Mr. **Robbins**. No, I am not suggesting that.

Senator **Ford**. Well, you just said that you were referring to the industry. I was just listening to you.

Mr. **Robbins**. I think my words were that there are isolated instances, and those are the things that I, as a good, solid, cable operator, decry.

Senator **Ford**. Well, isolated instances or isolated areas would be a franchise, and there are a lot of franchises, 9,000 of them. So you could have 8,500 problems, and they would all be isolated as this Senator sees it.

I have seen all of this selling going on and it's as high as $2,500 per customer.

Does that sound right? That's $2,500 per customer.

I didn't know I was worth that much.

Would you like to buy my residence? You can have it for $2,500.

Well, I've got a lot of problems, and I remember when I first came up here the cable industry was just mom and pop and they were struggling. We were trying to help them.

And now, we find that you've got a representative here that's probably making $500,000 a year, and that's telling us that you've gone from mom and pop to "zillionaires," as my grandson would say.

And so, the times that you split your stock for TCI—I don't know—two or three times, it comes out to much better than government bonds, as you told the Chairman.

So, Mr. Chairman, I am very interested in where we are going here. I am pleased to be on the bill with Senator Danforth and others, and I look forward to the rest of today and to tomorrow.

Senator **Inouye**. Thank you.

Senator Gore.

Senator **Gore**. Thank you very much, Mr. Chairman.

I am not going to belabor this GAO study because I think Senator Ford pretty well demolished it.

I would say the audit that was referred to was a followup postcard reminder to the ones that did not respond. I hope we can hold the record open for more on this study.

In Tennessee, we have had the same experience that Senator Ford has had in Kentucky.

I am going to ask you to look at this chart of Tennessee rate systems.

[Chart.]

I referred to some of them in my opening comments.

The line down at the bottom is the 26 percent that the GAO found. That's across the bottom.

Now, again, that is higher than the rate of inflation over the three year period.

But look at what the major systems in Tennessee have done.

Now, Mr. Robbins, you don't have any of those systems, and I don't challenge your testimony at all about what Cox's experience has been in its systems. And, Mr. Malone, I don't think you have any of those systems.

But look at what my constituents are paying. Over the last three years, since the rates were effectively deregulated in 1986, we have had increases in all of the larger cities of Tennessee of over 100 percent. Well, one of them was just slightly under 100 percent. These were 115 percent, 116 percent, 117 percent.

Is this okay, Mr. Mooney? Is that the marketplace at work?

Mr. **Mooney**. It's hard to comment on things like that without knowing something more about the fact situation.

Senator **Gore**. It came from the Cable Television Fact Book. You know the situation.

Mr. **Mooney**. If I could just give you an answer, in many instances, for example, when we have heard of very high percentages, we have found that tier consolidations, for example, have been part of the picture, where, say, 20 percent of the subscribers took what amounted to a kind of scaled down antenna service and 80 percent took the full service. Then they eliminated the scaled-down service, and the result was that, for some people who wished to continue with cable, a very high increase occurred.

I think, not incidentally, a lot of operators who did that, who consolidated tiers like that, have lately decided that that was the wrong thing to do, and are recreating some of those more basic tiers.

Senator, we do not argue and we do not deny that in some places some people abuse their freedom. That happened in some places in your State.

Senator **Gore**. Well, this doesn't even cover it. This is not the horror story. We're going to hear about the horror story later.

The Multivision rate increases are not even included in this graph. We're going to hear about those with the next panel.

Now, one of the systems involved here actually reduced the number of channels involved. Two of them, let me say, in Chattanooga and Jackson, added some services during this period. In Chattanooga there was a 115 percent increase and in Jackson there was a 68 percent increase.

But the others didn't. The others didn't add any services, and, as I say, one of them actually reduced services.

Now, you say that in 1989, using the same statistics, that the rate increases have flattened out. Well, I submit that they have just started to flatten the customers.

And in the Multivision case, we are going to see that in just a moment.

Now, let's talk theory for just a minute, Mr. Mooney. Isn't cable television a natural monopoly?

Mr. **Mooney**. Cable television undoubtedly has some of the attributes of a monopoly, most notably that in most places there is but a single licensee. I don't know that we've ever had a chance to find out if it is a natural monopoly or not, because the cities have never allowed us to find out.

Senator **Gore**. Oh, there have been a few attempts to overbuild, haven't there?

Mr. MOONEY. Oh, sure. Right in your own State there are five overbuilds going on that I know of right now.

Senator GORE. Well, in the case of an overbuild, can a new operator trying to compete with an embedded operator get access to exactly the same programming as the embedded operator?

Mr. MOONEY. In most instances, yes.

Senator GORE. Well, that hasn't been the case in Tennessee.

Let me just ask you this. If a group of local entrepreneurs decides to build a system in a town like Murfreesboro, where the rates have gone up 117 percent, are you telling me that all the programmers who now sell wholesale to the current operator will be happy to provide the same product to the new, competing operator on identical terms and rates?

Mr. MOONEY. Most of them have done it in other places. I do not know, of course, the specifics of the distribution contracts being held by the current company.

Senator GORE. On identical terms and rates?

Mr. MOONEY. I don't know. I can't tell you that, sir. I don't know what the existing operator's contract says.

Senator GORE. Do you know that the large multisystem operators commonly get a vast discount on the programming that costs much, much more to a small cable operator?

Mr. MOONEY. I don't know. I hear—

Senator GORE. You don't know that?

Mr. MOONEY. I don't know it, sir.

I hear people say it here all the time, and my friends, who are the MSOs, tell me that that is vastly exaggerated.

Senator GORE. Mr. Malone, don't you pay more for most program services than a small cable operator?

Mr. MALONE. It varies widely from service to service, depending on when the contract was entered into and the nature of the service.

Some services, like BET, TNT, we pay exactly the same. For the football surcharge, we pay exactly the same.

Senator GORE. Do you pay less for most of them?

Mr. MALONE. We probably pay less for about half, and about the same for the other half. Yes.

Senator GORE. All right.

Now, Mr. Malone, do you believe that you own too many cable systems?

Mr. MALONE. I don't believe that. No.

Senator GORE. I'm not surprised at your answer.

Would you believe that there is some justification for the Congress putting a limit on the number of cable systems that a company like yours can own?

Mr. MALONE. Yes, sir.

Senator GORE. You do?

Mr. MALONE. Yes.

Senator GORE. Where do you think that limit ought to be?

Mr. MALONE. I'm not sure. You know, it depends on how you count, I think, to some degree.

But, you know, broadcasters right now I think can own 25 percent of the market with VHF stations and up to 50 percent with UHF stations.

Our technology is different. Clearly, some lower limits are in order for our industry.

Senator GORE. I think that is an important point, Mr. Chairman.

Now, Mr. Malone, would you believe that it is reasonable for the Congress to enact limitations on the trafficking in cable television systems?

Mr. MALONE. Yes.

I would strongly support that.

Senator GORE. All right. Very good.

Would you believe it is reasonable for the Congress to reimpose some regulation at the Federal level?

Mr. MALONE. I don't know. I think there is some regulation at the Federal level now.

You know, one can argue about which markets. But the FCC has imposed some regulation.

There aren't a lot of subscribers affected, but there are a lot of systems affected at the present level.

To expand that in an intelligent manner, I would guess that that is going to happen. As the quality of our services improve in the industry and people regard it more and more as a necessity, I would expect that the government will increasingly want to have a say in rates and charges until they become convinced that there is adequate anticipatory or real competition that does naturally limit.

I think, Senator Gore, our market system works in a wonderful way, and while people can be excessive for a little while, technology moves on and competition moves on, and ultimately competition does represent the real limit to prices.

Senator GORE. All right.

Now, do you think that part of the problem we are dealing with in this hearing today could have been avoided if the FCC had been more aggressive in using the regulatory authority contained in the act?

Mr. MALONE. That's my personal opinion. Yes, sir.

Senator GORE. You believe the FCC has done a poor job in this area over the last three years?

Mr. MALONE. Well, I hate to be put into a position of criticizing a body that regulates me, but I think they could have been more active.

Senator GORE. I think this is significant testimony, Mr. Chairman. The largest operator in this business has said that he feels it is reasonable to impose limits on horizontal integration, reasonable to expand Federal regulation of the industry, reasonable to conclude the FCC has not been aggressive enough in protecting the consumers, reasonable to impose legal limits on the trafficking of cable television systems.

Now, what about vertical integration?

Do you think that your size and power have made your company arrogant and heavy-handed?

Mr. MALONE. I don't beat my wife, either.

No. I honestly do not believe so.

I think that the actions that we have taken have been almost entirely, well, they have been entirely really trying to serve as honest purchasing agents for our subscribers.

Senator GORE. Have you ever threatened a locality in connection with a franchise renewal?

Mr. MALONE. Well, I don't know what constitutes a threat.

I think we have indicated that if we don't get renewed, under Federal law we cannot continue to serve.

Senator GORE. Well, let me read to you from court testimony what I think constitutes a threat.

One of the top people in your franchise renewal department, according to court testimony, "threatened a consultant hired by Jefferson City, Missouri, saying, 'We know where you live, where your office is, and who you owe money to. We are having your house watched. We are going to use this information to destroy you. You made a big mistake messing with TCI. We are the largest cable company around. We are going to see that you are ruined professionally."

Are you familiar with that case?

Mr. MALONE. I lost an awful lot of sleep over that one, Senator.

Senator GORE. You were fined $25 million in punitive damages?

Mr. MALONE. That's correct, in a civil antitrust case.

Senator GORE. It was $10.8 million in actual damages; judgment affirmed on appeal; U.S. Supreme Court declined cert.

Correct?

Mr. MALONE. That's correct.

Senator GORE. Is that an aberration?

Mr. MALONE. That's an aberration.

Senator GORE. What about your conversation with NBC on their efforts to launch a competitor to CNN?

Did you advise NBC that it would not be a good idea for them to try to start an all-news channel?

Mr. MALONE. There is a very long history to our discussions with NBC about news. It goes way back.

Initially, and this is probably five or six years ago, long before Mr. Wright's era, they approached us and other members of the industry with respect to our interest in carrying and paying for a news service.

We indicated and had considerable discussions with them about the economics involved, about the likely success of such an enterprise, and our willingness to try to carry and support such an effort.

They did an extensive market test to see if there was sufficient demand for the service in the cable industry, and concluded that they could not get enough support from the cable industry at that time.

They were looking for commitments—if my memory is correct, they were looking for five year commitments at 15 cents, going to 20 cents a month a subscriber—we pay them—and they needed 20 million commitments in order to launch their service.

They didn't get there. So they abandoned the project.

Several years later—and I might say that a lot of that sense of an opportunity on their part was the result of what appeared to be some radical rate increases on the part of CNN, which was trying to increase its cash flows to pay for a lot of expenses related to CBS and, subsequently, MGM.

Senator GORE. Okay.

Mr. MALONE. That was at that time.

Then, subsequently, Mr. Wright, who I regard as a good friend of mine, called up and said NBC is very interested in getting into cable programming now and what do you think would work?

We kicked it around and said that perhaps what the industry could use and NBC would be most adept at supplying would be a service that was financial news during the business day and sports the rest of the time.

In talking about how one might go about successfully launching such a channel, I suggested that the most successful approach currently would be to try to acquire a semi-moribund or nongrowing service and convert it to this kind of service. In that way, one would secure channel capacity availability at the same time as introducing a channel, and that would be most appealing to a cable operator since cable operators generally are booked well ahead in terms of channel capacity.

Subsequently, Mr. Wright negotiated to lease from us a channel that we had acquired as part of some larger acquisition.

We paid I think $18 million for the channel and we leased it to Mr. Wright, to NBC, based upon an $18 million valuation.

We signed a long-term affiliation agreement with NBC based upon financial news during the day and sports the rest of the time.

Subsequent to that, NBC acquired a 50 percent interest in a national sports channel, called "Sports Channel America." They came back to us and said that they wanted to change the format. Since they now had a full-time sports channel, they didn't really want to go forward with the prior format that we had contractually agreed to.

We acceded to that by agreeing to allow them to change the sports component over to a broad consumer news type of service, which they thought, from their market research, and we thought would add something to the panoply of cable services.

We are and continue to be their largest affiliate in CNBC. We think they are doing an excellent job, and we hope that they get broad enough distribution to be successful.

Senator GORE. My time is running out, but I wish to clarify this matter for the record, Mr. Chairman.

Here is what happened as best I can analyze it from the facts.

The most profitable broadcasting network in America, with an extensive worldwide news gathering operation, attempted to launch an all-news cable channel in direct competition with CNN.

Mr. Malone, who controls 20-some-odd percent of the cable television systems in America and also owns a portion of CNN, advised NBC that, in his opinion, they couldn't get on enough cable television systems with a competitor to CNN; advised them, instead, to compete directly with FNN, Financial News Network, one of the few remaining independent programming channels.

NBC dearly wanted to go into an all-news channel. They were blocked from doing so principally by the opposition of the largest multi-system operator.

Now, he may not see that as anti-competitive. In my view, when someone who controls a quarter of the marketplace advises a potential competitor for one of his properties that they cannot break into the marketplace, the sheer size and power coming from the vertical and horizontal integration of this company is intimidating to the would-be competitor.

Now, he sold NBC for almost $20 million a moribund, in his words, worthless in my words, program service on the theory that it had some markers down in cable systems all over the country that made it worth something.

NBC let all those markers lapse and didn't use them. But, by giving almost $20 million to TCI and redesigning its format so it did not compete in any way with any of the properties, programming properties, owned by TCI, then Mr. Malone was forthcoming and, indeed, he is now the largest carrier of CNBC's redesigned service.

Now, what happens?

The public is deprived of competition in sources for news. They have only one all-news cable network.

I think that the public interest is not well served by this kind of market power, this kind of vertical integration.

Now, I would like to get to the satellite dish issue, but I'm out of time. And, you know, that is the issue that I'm most concerned about.

So, hopefully, we can have a second round, if possible.

Thank you, Mr. Chairman.

Senator INOUYE. Thank you.

Senator Gorton.

Senator GORTON. Thank you, Mr. Chairman.

I would like to ask each of you to comment, if you will, on what you consider effective competition to be. Whether you consider the definition of effective competition, which the FCC has adopted, you know, really, to be that.

And, in addition to that, if you will, tell me how we here in Congress, who obviously are concerned about the present situation, should operate and should legislate, if it is our goal to provide potential subscribers to alternative sources of broad band programming, such as the kind of programming, which cable systems provide now.

Mr. MOONEY. Let me take it, first, Senator. I think effective competition is the presence of substitutable services, which operate to create a check on cable pricing.

In other words, in the words of the economists, something that prevents the extraction of monopoly prices, prices beyond the true value of the service that is being provided.

And, I think, it is very hard to say with scientific certainty and certitude, that any standard, which is adopted by the FCC is going to continue forever to remain an adequate measurement of what it is that is going to prevent, you know, that is going to operate as a check on cable retail prices.

The last time this was done, which was in 1985, in which only one of the parties filing before the commission presented econometric evidence as to what an appropriate standard for effective competition should be, that was us, as it happened.

And I understand that the commission probably within, even a few weeks, will undertake an inquiry to re-consider, or at least, reexamine what it did in 1985, and consider whether that standard ought to be modified in some way.

And, you know, I do not think we live in a static world, either with respect to cable television, or with respect to other providers of television either. And it may well be that that standard may need some adjusting in light of the fact that this is now, and that was then.

What was the other part of your question?

Senator **Gorton**. Well, the other part of my question was, that if we or this senator believes that effective competition requires, or should encourage, the availability of more than one provider of the broad spectrum of programming, now provided by cable in, at least, most major markets.

How should we go about legislating in order to create that condition?

Mr. **Mooney**. I think it is very hard to do that, unless you are willing to start treating television programming, essentially, as a commodity.

And, I think that we would caution you very strongly against doing that, unless you saw overwhelming evidence of an overwhelming problem.

I think that you—as has been mentioned here earlier today—you have a much greater diversity of television programming available to the public that was the case within recent memory. If diversity of viewing opportunities and diversity of program sources and diversity of T.V. experiences is an important public objective, we think that it helps the public interest not to move into these areas and start regulating program distribution, unless you are really in extremis. And we do not see that that situation exists today.

Senator **Gorton**. Mr. Malone and Mr. Robbins.

Mr. **Malone**. I would say that in various segments of our business we do face direct competition in the service to apartment buildings, for instance, satellite receivers do represent day to day competition for virtually all of the cable services to a cable company and pay T.V. services, which are principally driven by movies.

Video cassette rental stores represent direct competition and have been an effective price check on rates charged for pay television options.

In terms of what Jim calls sloppy service and gouging rates, what happens there, the enzymes do not work as fast, perhaps as we all, and particularly you all would like to see happen.

And when rates get too high, and service gets too sloppy, the industry has demonstrated that the competitive cable systems do come in and begin to get built. And, it usually results that owner being changed and the service being improved and the rates being moderated.

So, in that sense, anticipation of competition does serve as a check on rates.

In the case of satellite receivers, when cable rates get somewhere in the low 20s for the basic services, one would see, in my opinion, a rapid growth of home satellite receivers at C-band.

Even at the present retail prices available to back-yard dish owners, and that if the technology, if there is a market demand created by that kind of profitability vacuum, K-band receivers would come into play and would limit cable to some pricing in real dollars, somewhere in the low 20s, in my opinion, and be effective competition for all residential customers.

So, it is sort of—there is no easy answer. And I believe that it is not economically viable to sustain two wires into the home providing, essentially, equivalent services. Because all you do there is double the capital cost, double the operating expenses, or raise them by 150 percent and split the revenues in half.

And, unless you want to contemplate substantially higher revenues, you are unlikely to get an economically viable solution on a permanent basis with two cables. But you are likely to arrive, and not too far in the future, at a viable competitive posture of a balance between satellite and cable for residential customers.

It probably has not happened as fast as some people would like. But with seven applicants for K-band satellites with the wholesale pricing and retail pricing of satellite packaging now coming down, I think that you could predict that that would be the situation in a couple of years.

Senator STEVENS. Mr. Chairman, would you yield for a request?

Senator GORTON. Yes.

Senator STEVENS. Mr. Chairman, I have a conflicting meeting and would like to make a suggestion, a request of the Chairman. And that is to extend to the people on each of these panels the opportunity to file with the committee, comments on the Danforth bill.

So, that we might have them over the coming recess. So that we can study the points of view of the various witnesses, who will be here today.

I would have gone through some litany similar to what Senator Gore did in reference to the Danforth bill. But I do not have that time, and I do not think the committee does.

I would like to see, on a voluntary basis, if the committee would receive comments from these witnesses on the Danforth bill and share them with members of the committee. So that we can study them over the Christmas recess.

Senator INOUYE. That request will be conveyed to all witnesses.

Senator GORTON. I have no more questions, Mr. Chairman. But Mr. Robbins is here to answer my last question.

Mr. ROBBINS. Senator, I would like to share with you two very real life experiences in Spokane, Washington.

In 1984 our system was languishing there in the maybe 40 percent penetration level. Since the Cable Act, we have added a considerable amount of new programing in that system.

And our system, I can tell you now, is up in the mid 50 percent kind of penetration level. I cite that to tell you that if we had not added that programing, we would not have the kind of penetration that we have in there today.

We are moderate in the revenue—again, we are, there like in all of our places, we are moderate in the revenue that we bring out of the home and are very conscious of that.

You have to be more so in those markets, where the penetration is low, or the consumer is not going to step up and see the price value relationship.

I want to share with you one other example, to which Mr. Malone referred, and my comment was excessive rates, not gouging or whatever. That word did not come from my testimony.

There is a situation adjacent to one of our systems in Florida, where the service provider that has disrupted Mr. Gore's state, state of mind so greatly was, indeed, providing lousy service and had raised its rates inordinantly.

And, while I am not proud of this, we have gone in to that community to provide an alternative to this operator that was not doing the kind of job that he should have.

Senator GORTON. I do note, Mr. Robbins, that in the three years, since 1986, your rates in Spokane have increased 59 percent.

Mr. ROBBINS. Is that the basic rate that you are referring to?

Senator GORTON. The basic cable service, yes.

Mr. ROBBINS. We have added a number of new channels in there. And what we really look at is what is coming out of the average consumer household. And the comments that I made in my opening statement were that our average compounded increase was 3.75 percent from the period 1984 through 1990.

Our projections from 1989 to 1990 are 4.4 percent.

Senator GORTON. Nonetheless, that is why we are here today. Mr. Chairman, I thank you.

Senator INOUYE. May I now call on Senator Pressler.

Senator PRESSLER. Thank you, Mr. Chairman.

Mr. Mooney, NCTA represents both large and small cable systems as I understand it. Do some of your smaller members who suffer from the practice of volume discounting want some legislative relief?

I know that many small cable operators in my state want legislation, such as that which I introduced in January of this year, S. 168.

What do you hear from your smaller members on this volume discounting issue?

Mr. MOONEY. I hear a mixed message. I hear a few of the smaller operators say that they would like some legislation of that kind. I hear an even greater number of small operators say they regard that as a problem, but they would rather not see the government enter this area and would be against that.

Senator PRESSLER. Well, if the government does not enter that, how will the problem be resolved, the problem of volume discounting? I know that we all want to see the market work its forces. But some of the market is not working.

And if the government does not enter, how will the problem be resolved?

Mr. MOONEY. Well, I should say that I represent not only large and small operators, but programmers too, and see that perspective as well.

And there seems to be a fundamental difference of opinion here as between programmers and some of the small operators. Whereas the smaller operators want to be able to get together in a cooperative and buy programming on an aggregate basis, particularly from the pay services, and get what they understand to be the same volume discounts, as are given to the larger operators.

I am not sure, incidentally, in all instances that they are correct in what they anticipate are the magnitude of those discounts. But, in any event, that is all they want.

And the programmers say, well, you know, there is not much in there for us. Because we do not expect that we will get any additional subscribers. That, essentially, we will get the same subscribers that we get from you now. But that we will simply get less money for it, and why should we do that?

And, so, you have got kind of an impasse over money and the trade association really is ill-equipped to take a position in that matter.

Senator PRESSLER. Mr. Malone, your company has been especially successful. What percentage of America's cable subscribers do you reach through systems you own or have an interest in? And how many of your system have competitors, that is, from cable or wireless, from other cable, or wireless? I guess it is sort of a two-part question.

Mr. MALONE. I would think that measured the way you are describing, we probably have about 21.5 percent of the cable industry, maybe 22 percent.

In terms of competition from, as you are defining it, MMDS perhaps as wireless.

Senator PRESSLER. Yes, or cable. I mean, I know you——

Mr. MALONE. Cable is—cable over-builds in our experience are quite limited. I think we have six or seven areas in which there are multiple cable systems operating or being built. But there would be a minuscule percentage of our total subscribers.

MMDS, I would think would be fairly substantial in terms of subscribers, because it exists in some of the largest markets that we are in.

And, therefore, on a subscriber basis would be probably 20 percent, I would guess, of our subscribers have the alternative of MMDS service.

Senator PRESSLER. Now, you said it would be proper to cap the size of multi-system operators. Where would you cap them,?

I would also address that question to Mr. Robbins.

Mr. MALONE. That puts me in an awful position. You know, if it was me, I would cap it at 25 percent, or 21.5 percent. Or, if I had to go for a lower number I would say, since the company, the only company that it affects is mine, I would say that the government should be, since it would represent a reversal of government policy, should be very understanding and should put the pressure for divestiture in the most pleasant of terms, let us put it that way, in terms of time, in terms of tax impact, in terms of other issues.

You know, that is a decision really for you, gentlemen. And the rate is—market power, I think is an issue that if you find that we have too much market power, you know. We do not feel we do, but if you feel that we do, well, you know.

You tell us what we should do. But do not make—do not render this industry nothing more than a collection agent for programmers. Because right now, we are very vulnerable to just being nothing more than a collection agent.

And as we have very little ability to resist price increases on many of the services we provide.

Senator **Pressler**. That intrigues me intellectually.

You feel that the industry would become a mere collection agency for programmers.

Mr. **Malone**. If it was fractionalized to too small a level and did not have some bargaining power left, yes.

Senator **Pressler**. Do you think the programmers are abusive in their power?

Mr. **Malone**. By and large the programmers have been very, very good to-date about coming to us, explaining why they needed the money, why they needed the increases, and supporting those increases with improvements in the quality of the programming delivered.

There have been some abusive situations. I can go back, Senator, to around the time of the cable, though a little before, when services that had come to us and gotten on our systems on the basis that they were going to be fully advertiser supported and would never make a charge, okay, proceeded to implement very large charges on a take it or leave it basis.

And some of them even capitalized those increases and sold their companies at huge profits. And that practice is really what drove TCI.

Up until that point we did not regard it essential that we have either long-term contracts, or equity positions, or a way to keep a balance.

That scared us so badly in terms of what it did to us. I am talking dramatically. I am talking about going from zero to 50 cents over three years for a service that was one of our most popular services.

And the company that owned that service filing proxy statements with the FCC to go public based upon those projections. That kind of abuse is what scared us and drove us into vertical integration, or long-term contracts.

I mean, so, I think—excuse me, for a long answer. But the problem that I feel is that we are a purchasing agent primarily for our subscribers, and if we do not have some market power to perform that function, we will be really rendered just a collection agent and a pass-through vehicle.

And perhaps that explains to some degree the scramble for vertical integration into cable channels, because people see that opportunity. And in some limited cases have already abused that opportunity.

I think the Madison Square Garden, New York example, is a very real example of that kind of power and that kind of abuse.

Senator **Pressler**. Mr. Robbins, do you have any comment on that?

Mr. **Robbins**. Well, as an individual responsible for maybe 3 percent or less of the subscribers in the cable television industry, the horizontal issue is not really one that I have given a tremendous amount of thought to.

I would suggest in Mr. Malone's defense that he has indeed helped hold down prices for a number of these services that have wanted to do things that were not in the public interest.

So, I take maybe a different slice of that.

Senator **Pressler**. Thank you, Mr. Chairman.

Senator **Gore**. Senator Kerry.

Senator **Kerry**. Thank you, Mr. Chairman.

Mr. Chairman, I unfortunately have another meeting that I had to be at about 10 minutes ago. So, I cannot pursue, as much as I would like, here.

And I take it that the record can remain open for the submission of written questions and more information and data.

Senator **Gore**. Yes.

Senator **Kerry**. I have not yet signed onto any of the bills that are in the committee. And I think it is very important that the committee, I think these hearings are very important. And I think it is very important for us to continue carefully to collect yet better analysis of precisely what is happening in this marketplace.

I say this because, while obviously there are some egregious incidents that I think you and members of the industry have acknowledged, I do not think it is yet clear to us precisely what all the patterns are.

And I would not be happy with the notion that the committee is going to create a new framework without totally understanding the current one.

Let me be precise about, perhaps, one of those questions, as it looms to, at least, this senator.

I wonder to what degree some of those price increases in Tennessee and in Kentucky and elsewhere may or may not have been the result of a process that forced a competitive bidding process that created a lot of unreality at the outset.

And given the early regulation that there has been a certain amount of adjustment in the process since that deregulation. Now, in Boston and in Massachusetts, the state decided to experiment earlier on deregulation than in other places.

And beginning in 1980 there was a deregulation so that there has been a slower process in the increases. But just to underscore what I am saying, while there has been a 76 percent increase in Massachusetts cable fee, Boston's basic fee in 1986 was $2. And it is now $15.95 cents, that is a 698 percent increase.

And that came about, obviously, because in the early bidding process people just made bids that were wholly outside of reality in order to get the franchise. And because of the lack of regulation, this was permitted to happen, and it is now history.

I do not hear people in Massachusetts, and maybe by saying this, I am going to invite that complaint, but the fundamental complaint is not about prices right now. It is about service.

And people are upset with the notion that they have to wait for days to get somebody in, because there is only one person to call, and the phones are always busy. And they cannot seem to get the service that they think they are due. But they do not seem to feel that the service they are basically paying for is somehow unfair.

Now, one of the fundamental questions here is, therefore, how many of those systems out there, are the result of the early process. How many have gone through changes in programing and capitalization and instructure, which have mandated an increase simply to survive. And how many are gouging?

And I think the committee and the industry have got to try to work somehow to get that answer, before we try to address the issue. That is one feeling. Maybe you want to address that question overall.

But one of the fundamental issues, I think, here is this question of defining monopoly. And to a degree that depends on whether or not there are other means of providing news, providing sports, providing entertainment.

Let me, again, be specific. In North Adams, Massachusetts 93 percent of the homes there receive cable. There is a mountainous area, what we call mountainous in Massachusetts.

And in Boston only 39 percent of the homes take cable. And obviously to me that says something about the availability of other forms of entertainment, news, home video, sports, live and otherwise.

Now, do current FCC rules take account of anything besides the number of over-the-air stations in determining this definition of monopoly and penetration?

Mr. MOONEY. They have been revised since the original rule making to make sure that the signal actually is available in a place.

In other words, revised from theoretically available to actually available. Otherwise they have not been revised.

Senator KERRY. Is it possible that we should think about looking at—can penetration alone tell us where there is effective competition?

Mr. MOONEY. I think penetration obviously has a bearing on it. If you see a place where the cable penetration is 90 percent, yet the national average penetration, where we do actually have franchises is 60 percent, 90 percent tells you something about necessity, as distinguished from simple choice.

But it is very hard to pin down precisely what a given penetration level, which you could describe as being a kind of threshold, where competition falls, you know, absolutely falls off.

That is not to say it cannot be done. I am just not sure, if anybody has ever tried it.

Senator KERRY. Well, do we, as we approach this issue, as this committee thinks about it, do we need to think about a moving standard with respect to this question of competition and monopoly? And how we begin to divide it up? Or can you have a uniform standard?

Mr. MOONEY. I think that, you know, without getting into a situation, where we are endorsing legislation, because we do not mean to, we are not at that point, we believe that you should think of, not only fairly sophisticated standards, but you have to think in terms of what you mean by regulation.

You know, city council regulation never was regulation in the sense that that term implies public utility regulation, in the sense that it implies a coherent underlying intellectual discipline.

It was always rather chaotic and arbitrary and did not really have the benefit of an underlying discipline. It is not—it was never regulation in the sense of what goes on in state public utility commissions or in the FCC.

It was pretty much, do you want to vote for a rate increase? "No. Why should we do that? Vote it down." That is why we ran 72 points behind the CPI over the 14 year period the FCC let them regulate the rates.

Senator **Kerry**. Well, I want to explore that more. I am not going to do it now. But I think that we need to think hard about that definitional problem.

Mr. Robbins, let me ask you, with respect to the question I raised about service. The fact that people do not have a choice about which company they call, what can be done, in terms of that increasing complaint factor that we hear?

Mr. **Robbins**. I commend your understanding of where most of the noise is coming from on the service side, rather than on the rate side. And I think what we have to do is to buckle down and get the installations done, when we say we are going to get them done.

And in a very short amount of time after somebody suggests to us that they want it. We are, as I said in my opening statement, and I do not want to repeat it to take up time, but there are a number of standards of service that this industry can get onto.

And, I think, many, many, many companies in the industry are getting on to that. I think we have a special responsibility to do that.

So, I do not know whether that is the kind of answer you were looking for to your question. But we are hard at it in the industry, and particularly in our company. And I think that is the way we have to go.

Senator **Kerry**. Another significant concern in Massachusetts, and I think it is shared elsewhere, obviously, is the preservation of sports programming choices. Frankly, there has been an enormous expansion in New England of available sports programming.

And we can get home games that were formerly blacked out and so forth. So, I think, it has been in many ways a huge success in that.

But a lot of people are concerned about how long that may last. And there is a certain migration that is beginning to be perceptible.

Should we be dealing with this issue as we approach—I mean—should we create some protection, as we begin to rethink the act against the further migration or in setting limits as to the migration?

Mr. **Mooney**. I think what you have got going on there, is a situation where the owners have found out that by putting the rights, essentially, on the auction block, they can get a lot more money.

And some of the cable networks that are sports oriented, for their own competitive reasons vis-a-vis each other bid for these rights.

I do not fault them for doing that. Not only because I represent them, but because they think they have a right to live in the world too, and to be successful.

But some of the other programmers look at that as just drying up what new money there is for programming. And most of the operators I know look at it as just putting them into a squeeze, because they basically have already got everybody who is a sports fan.

You do not really get any new customers, I think, for getting more sports. What you get is added programming cost, which means it puts upward pressure on basic rates for everybody.

So, I think that you find a lot of people in the cable industry who are as unhappy about that, as I know some members of this committee are. And there will be people in my industry who chastise me for saying that. But it is the truth.

Senator KERRY. Is that an affirmation of the notion that we should look at it hard? About whether we should actually codify some kind of restraints?

Mr. MALONE. May I make a brief comment? I think that the real abuse and the reason why speculators, if I want to call them that, have come into this sports packaging area, is the practice of programmers of requiring the cable company to take it or leave it.

In other words, all customers who got to take it and pay for it, or you cannot have it at all. If these programming services were optional to the consumer, then I think market forces would limit what could be paid and a more legitimate balance would result.

That was the dilemma in New York City with the Yankees. It was not the question of, you know, offering the Yankees to those subscribers who wanted the Yankees at any price. It was a question—because if the price got high, fewer and fewer people would take it, and there would be an automatic limitation as to what that speculator or entrepreneur could do.

The proposition in New York was, if you want to keep the Knicks and the Rangers on cable, you got to take the Yankees. And you have got to take it for all your subscribers, and you have got to pay for it for all your subscribers.

That was really a massive price increase for programming in that market. And the cable operator was in this very tough squeeze position that Jim is referring to.

And in that market that was about a 60 cent one shot rate increase. It made us all feel very vulnerable to it happening again.

Mr. MOONEY. I owe you an answer on that legislative question. I would recommend you go to significant jawboning first. And if that does not produce a result, then, maybe think about something else.

Senator KERRY. Two quick questions before my time terminates. Mr. Malone, you testified before the committee in June, and I asked you then—incidentally, I had some questions about the vertical and horizontal areas, but I think I have been through that a little bit with you, and I do not want to belabor it now—but I asked you then about the take-over of Time.

And you had some comments at that point in time, that has now been insured by the courts and so forth. But now we see Columbia Pictures purchased by Sony. And I would just like to ask you, if you see some implications of this kind of development of a global communications firm?

Is something happening that we should be thinking about? And what does that mean for the consumer? And for America's role in global marketplace?

Mr. MALONE. Yes, I think a lot is happening. And I believe——

Senator KERRY. And finally, I suppose, does that also become part of the puzzle that we are looking at here, as we think about what we do?

Mr. **Malone**. I think it very much does. I think on a worldwide basis, we find our companies competing with foreign national companies, who are not only not limited in terms of what they can do, but encouraged in what they can do by their governments, to vertically integrate, to try and control through scale economics everything from one end of the cycle to the other, when it comes to intellectual properties.

And, I am terribly afraid that this vertical integration that is going on overseas with the capturing of vast international markets will come back over here and give those companies such enormous clout in terms of dictating technology, in terms of dictating supply and availability that American companies will have a very hard time competing.

I think this was the argument that Time-Warner made. As a little cable operator, or a big cable operator, the merger of Time and Warner is a scary kind of a thing, because it is an enormous accumulation of power.

As an American, I think, I see no alternative but for our country to allow our industries to go this route in order to be competitive worldwide.

But, unfortunately, the impact in our corner of the world is to scare the hell out of us in terms of, you know, is their power going to be turned on us. Are we going to be cannibalized.

So, you know, I think, government, you know, in our kind of a society, it was all wonderful when there was no over there. When we set all the rules, and we all abided by them. Small operating units, ma's and pa's, local regulation, a slow moving world, a slow moving technology could survive.

I am afraid that in the future, if our industry is Balkanized, we will not be able to play any material role in the creation of intellectual property, which is becoming a substantial export now, to play any effective role in this evolving technology of high definition.

I mean, the most potent thing we have is our market size, our scale economics in this country. If we Balkanize that we are really giving away the last true competitive advantage we have against international competition.

So, I guess, as a citizen, I would hope that in doing this kind of thinking, this committee does not so strip our domestic organizations of their scale economics collectively that, you know, they really cease to exist.

And that they then become in fact nothing more than small bite-sized prey for multi-national companies choosing to vertically integrate downward here.

Senator **Kerry**. Mr. Chairman, I just want to underscore that I asked that question, obviously, because I think it is of major consequence to what we do here, and what is happening in our communications industry, in fact, in all our industries now.

We have sat around in Congress for a number of years now bemoaning our competitive posture, recognizing the cost of our capital relevant to other countries, and continually shooting ourselves in the foot, while our corporate entities are trying to compete against nation states.

And, I think, respectfully, that we have got to decide what kind of playing field we are going to be on. And I think the choices we make in this are part of that larger question. And I simply want the committee to try to come out on that on the reasonable end.

I do have some other questions. But I think I have abused my time. And I thank the chairman very much.

Senator Inouye [presiding]. Thank you.

Senator Burns.

Senator Burns. Thank you, Mr. Chairman.

First of all, I want to thank you for holding these hearings.

I guess, as we follow the rhetoric today, I think we want to take a look and see—I think Senator Kerry hit the nail on the head—in which direction we should be going.

First of all, when we talk about rates and all of this, let's put all of that aside for a little bit because, let's face it, nobody is holding a gun to anybody's head to sign up on cable. It's a free market out there.

I almost changed my mind the other day.

But I think in these hearings and what's ahead of us, we should get from these gentlemen here, who have spent their time in this industry, their comments on just about every section of Senator Danforth's bill and how you view it.

I happen to be a co-sponsor of this legislation. I don't think there is anything written in stone as the dialogue continues.

I think there will be some changes made and we hope it will be for the good of everybody.

But these hearings stem, in large part, from some alleged abuses by the cable industry since 1984.

Many people now refer to cable as an unregulated monopoly. We have heard that.

In order to deal with the so-called cable problem, two solutions, as far as I am concerned, come to mind: either reregulate the industry or expose it to competition from multi-channel providers, such as, and it hasn't been mentioned here yet, the telcos.

I would like to hear the comment from maybe all three of you: which of the two courses do you favor?

Mr. Mooney. That is like being asked whether you want to be boiled in oil or vinegar.

Senator Burns. I know that is sort of a loaded question. But I think we are going to come down in this place to where we are going to have to make some choices on in which direction we want this industry to go.

Mr. Mooney. I would just offer the comment—and I hope you won't make me choose between those things—that I think the implications for this society of allowing telephone companies to get into the TV business go way, way beyond any issue of cable television.

If you look at the industry literature in the telephone industry, you will see what they have in mind is that they should not only use one wire for the provision of telephone and television service, but that they should effectively be the only transmission facility for television service.

To borrow a phrase used by the FCC's Office of Planning, even the broadcasters should take down their red and white towers. To create a circumstance in which telephone companies were providing all electronic communication into the home, supplanting all other existing electronic distribution facilities and then also to allow the telephone companies into content I think has implications for the democracy that are poisonous and that go well beyond any problem the Congress may have with cable TV.

Senator **BURNS**. Mr. Malone, would you like to respond to that?

Mr. **MALONE**. Yes.

I think that rational people would say that there is a balance here.

In some situations there should be some regulation and ultimately technology moves on. Nothing is forever, not even cable. And there will be competitive services evolving. They are already there. They are just not quite price competitive yet.

I would not put this industry in such a box that it cannot follow evolving technology because that is our job. I mean, we are supposed to stay competitive and stay up on technologies.

I would say that it should be a balance.

On the telephone issue, having been educated by the telephone industry, Bell Labs and AT&T, in fact, at one point having been called a "deep plant" of the telephone industry in the cable industry, in some "Manchurian Candidate sense" I believe that there will never be one wire into the home because it is not technologically or economically rational.

This has nothing to do with politics. It just has to do with two completely different architectures of information transmission.

Having said that, I think the real question, if the telephone companies are allowed in in their own operating areas, is are they going to end up owning both of them because I think that that would be the result there. I don't think that that is what you guys really have in mind in terms of spurring competition.

In my own opinion, Senator Gore has been on the right track—you know, make sure that programming is sort of available; that people don't tie it up too exclusively for too long; that an industry that is in power for the moment does not squash new technology so that it can ride out its existing technology too long.

I think that those are kind of the ways you manage this process. And this is a process.

Our systems do not last 15 years. Our systems last for five or six years, and then we go out and rebuild them and add channels and add services and put new equipment into everybody's house.

We have to write it off and then we have to go and do it again. That is why the return on assets in the business is so low.

You know, as far as monopoly goes, I wish I could find monopoly profits in any of the operations of the business. The profits in this business so far have been pocketed by the guys who have speculated, who have bought and sold, but not by the people who have hung in there and reinvested in their systems and tried to keep up with the technology.

That is kind of a weasel-wordy way of saying that I think it is a mixture, and I think the only proper way that this industry should be dealt with is by an entity that fully understands all of the relationships and imposes what controls and limits it does from a position of having really thought it all through and understanding what all the implications are.

You asked also for a reaction to the proposed legislation, and I guess, as a cable operator, I don't have a big problem with the must-carry provisions.

There is an equity issue there and there is also a constitutional issue.

The equity issue is between broadcasters and cable programmers in terms of channel positioning. The constitutional issue is whether or not it would get thrown out by the courts because it is an intrusion on the First Amendment. I am sure somebody would bring up that argument.

But, as a cable operator, I have no problem with that. Once this government has looked at the equity issues of channel alignment and says that we should give that kind of an edge to local broadcasters, I don't have a problem with that.

Cable programmers might, but I do not.

With respect to the limitations on our size, I think I have already addressed that. It seems like it is an "anti-TCI" thing. But if that is what the government wants to do, you know, it's my government, too.

On the issues of pricing and availability of programming, I think that a thorough review would indicate that, generally speaking, the system is working and the abuses are very limited to a few programmers.

I think if somebody could enunciate, like an FCC, what "fair" should be, I think you would find that people probably would line up and do what is fair in that area.

My biggest problem and I think the thing that would just absolutely shoot this industry in the head is returning us to local regulation without extensive Federal supervision and guidelines.

We would just be stopped dead in our tracks. We simply could not go back to 10,000 regulatory agencies every year to keep up with the cost of living. That would decapitalize our industry very fast.

Wall Street has already reacted to the possibility of this kind of legislation by taking 20 percent off the cable stock capitalizations.

I think it would be unworkable for our industry, it would be very difficult to raise capital, it would be very difficult to meet the demands of the Federal Government. In things like high definition, it would be very difficult to respond to subscriber needs.

So that section of the provision I find to be effectively a death sentence, as far as my long-term view of this industry. It would simply take what is a major emerging American industry and "balkanize" it to the degree that it could not keep up technologically or programming-wise. It couldn't do the job that I think we need to do for the American public.

I think that is basically it.

Senator BURNS. Mr. Robbins.

Mr. ROBBINS. Senator, you asked about competition from the telephone company.

I do not think that that is the answer for all of the reasons that Mr. Malone and Mr. Mooney have enumerated.

I just don't think that one wire, as they conceive it, with everything on it, is in keeping with the democratic principles of this country.

You ask is some form of reregulation in order.

I am not sure that we are at the point where we need that.

As I stated in my opening comments, the deregulation of rates is what has allowed the development of these vast programming opportunities. I have to tell you, when I was in a hotel in Helsinki last year and I tuned in and saw CNN, I felt very, very good that there was an American export that is being received over there.

I don't want that to stop.

I would come back to a comment that you made right at the opening of your statement. In our business, every day is election day. If the customer does not feel that the price-value relationship of what he is getting from his cable operator is satisfactory, he cuts us off.

Senator **Burns**. I sure think that if we go the competitive route and allow the free market forces to take their usual trends—how long do you think it will be before your industry goes to fiber and we get away from the cooper.

Mr. **Robbins**. We're doing that right now.

Mr. **Mooney**. Extensively.

I think that both of the companies that are represented in this room are extensively into fiber in their trunking. Where it is efficient to use fiber, we use it, and thus far, we have found it most efficient to use it in our trunking plant and in some of our feeder plants.

We don't think that it is necessary to take fiber all the way to the home. I don't want to give you too detailed an explanation of that, but perhaps I can make an analogy.

An inter-city eight-lane highway is great and very useful. But that doesn't mean that everybody should have an eight-lane driveway into his house, because there is not that much traffic going into each house all the time.

You're not running 100 TV sets at the same time.

But we do use fiber increasingly, and, indeed, some of the people in our engineering community believe that we will replace our trunking facilities with fiber before the phone companies finish that process with respect to their own.

Senator **Burns**. Let's head down one other avenue here, and I know that I'm taking up a little too much time here myself.

There is the issue of content and conduit. There is the vertical integration thing.

I remember when I went into the radio network business in Montana. I went out there and I found a microwave that had posted a rate with the Public Service Commission.

But do you know what? They found out that I was going to be in competition with a program service that they were feeding down their own microwave. And every time I showed up on their doorstep to talk with them about a business deal and about starting my own network, the office wasn't open.

I never did get to them. Finally, they made me so damn mad that I just went to an alternative service, and it was called the "telephone company."

It made me so mad that I went to the telephone company, paid a little bit higher rate, and dedicated to compete very heavily with these people. Now they are no longer in business and my outfit is still going.

Maybe that's what it takes.

But the point I'm making is that there was another service available to compete with that service. It probably could have been more desirable. But it allowed me to compete with those people, and that service was there.

I think that is what most programmers are looking for.

Do you have any ideas on that, on the difference between conduit and the ownership of the programming?

Mr. MOONEY. Vertical integration can be a good thing or a bad thing, and sometimes it can be a good thing and a bad thing at the same time.

One of the ways, in fact, the primary way it has been a good thing in the cable industry is that vertical integration has been the means by which we have stimulated the development of programming that was necessary to flesh out the promise of cable, the promise of our medium, when nobody else was really willing to step up and put up the money.

This Committee this year has taken testimony from the founder of the Discovery Channel, for example, which does documentary programming, in which he described going from place to place, even in Hollywood, trying to get people to put up money and nobody would do it, because that wasn't their kind of TV.

Bob Johnson, from Black Entertainment Network, has told the same story and observed that banks don't lend you money for this sort of thing. You have to get equity capital.

The only people that had a real incentive to do it were outside the traditional program creation industry in Hollywood. They were the cable operators.

Now, having said that, we understand, too, that vertical integration sometimes can be a bad thing in the sense that it can incent people to deprive others of entry to the market.

All we can say is at this point, we don't think there is any evidence that that has actually happened.

This year, we have presented data to this Committee in the form of a study done for us by Dr. Kline of USC who analyzed it and said that he didn't see any evidence that vertically integrated players were any more or less likely to carry other people's programming than nonvertically integrated players.

I don't say that that is a permanent condition. That could change, but it hasn't. In the absence of abuse, we don't think a remedy ought to be imposed, for fear that it would disrupt the further progress of the good side of vertical integration.

Senator BURNS. I would be interested in your written comments on this piece of legislation and your suggestions on how we could do that.

I will ask the same question of future panelists.

Thank you for coming today and thank you, Mr. Chairman.

Senator INOUYE. Thank you.

Senator Danforth.

Senator DANFORTH. Thank you, Mr. Chairman.

This panel has now been on for two and a half hours, and they are about to pass Oliver North's record for length of appearance before a Committee.

So I am not going to ask any questions.

I do appreciate the hearing. I think that the suggestion of Senator Stevens is a very good suggestion. We want to be fair. We want your suggestions relating to the legislation, and this will give you an opportunity to provide written answers, written positions on the bill that was introduced yesterday.

My own view is that it is in the best interest of everybody, including your industry, for Congress to act.

I don't think that introducing bills and then letting them hang for long periods of time would be in anybody's interest. A number of bills have been introduced. The one that was introduced by 15 Senators yesterday is just the most recent example.

My hope, Mr. Chairman, would be that we could receive these written comments and that we could, at an early date next year, hold hearings on the legislation itself and then schedule a markup.

I just want to make one comment on what has been said earlier by Senator Kerry and in response to Senator Kerry by Mr. Malone.

I have spent some time in dealing with problems of international competitiveness, and I must say that I just don't buy Mr. Malone's position at all.

I cannot understand how the competitiveness of the United States of America depends on the maintenance of a monopoly of the entry of information into the American home.

I think that competition is as American as apple pie, and that we have built a vital economy on the basis of competition, not on the basis of monopoly.

I think monopoly is the exception, not the rule, and that it must be the exception and not the rule, and that where monopolies must exist—and maybe you're right, that only one wire can go into the home—then that industry must be regulated.

An unregulated monopoly is anathema and must be anathema in the United States.

The concept of vertical integration—again, this is an issue that has been addressed by our anti-trust laws since the beginning of this century. Where the antitrust laws are not enforced and where we have an industry that is as important as the providing of information to the American home, it seems to me that that is precisely where Congress must act to provide that we do have competition, that we do not have price discrimination, that we do not have discrimination in the providing of services by programmers to the television service itself.

So, I really think that if the philosophical argument is that somehow the competitive stature of the United States is going to depend on unregulated monopolies, we have somehow gotten far afield of what we used to believe made America an economic star.

So, that was just the one comment that I had.

I thank you for having the hearing, Mr. Chairman, and I do hope that next year, not taking anybody by surprise—we have introduced the bill this year. We have had hearings this year. Everybody knows what the issue is. Congress is not going to act precipitously. Congress is going to act very deliberately, very cautiously.

You will have every opportunity to give us input.

But it is my hope that we will act and that we will act at an early date next year.

Thank you.

Senator INOUYE. I am a member of the old school of legislators who usually follow the rule that regulatory law should be given time to see itself implemented, have a proper shakedown cruise. But all of our mailbags have been exceedingly heavy with complaints about shoddy service and excessive rate hikes.

I am certain that you can tell by the tone of the questions of the Committee here that something is bound to happen.

Having said that, I would like to refer back to something that happened many, many years ago, the Medicare Bill.

At that time, many of us felt that Medicare was bound to happen, and we called upon the medical profession to work together with the Congress to draft a bill that they can live with.

Instead, they spent all of their time fighting it, just opposing it.

And so, what came out was a measure that for the first decade or so, the medical profession I believe suffered.

I believe that, notwithstanding the pleas of your industry, this Congress—and I am not speaking of this Committee, but this Congress—will act on some measure that will bring about some reregulation.

I don't know what it is.

I have purposely stayed away from co-sponsoring any one of the measures here because I want to be able to look at it as objectively as possible.

The suggestion that we continue jawboning will not fly, believe me, because, unlike other groups, such as the professional groups, you have no self-policing agency or monitoring agency. So, no matter what we do in jawboning, these speculators, these buy and sell operators, will continue to operate. They will continue to increase our mailbag.

So I would ask you to be very careful in responding to the requests made by Senator Stevens that you comment on the measures before us.

I would suggest to you that a flat-out negative response really will not fly with this Committee.

There may have been a time two or three years ago when you could have, with justification, suggest that we haven't had enough time.

Now, I don't know whether five years is enough time. In actuality, I think it has been operating for about three years. And I don't know whether three years is sufficient time.

But we cannot close our ears to the shouts from our constituents. They are pretty loud.

I will very carefully study the proposals of Senator Gore and Senator Danforth because I know that this Committee, notwithstanding the old-timers, will act. I am just hoping that we will do the right thing.

We have in the past I think taken the wrong steps. We have reacted like knee-jerk politicians. We have overly reacted. We have been overly restrictive.

For one example, at one time our shipping industry was number one in the world. We controlled the high seas. We are number 14 at this time. We carry less than 5 percent of our international cargo.

I think some of that is due to our restrictive regulatory legislation, and I don't want that to happen to you.

Therefore, we will need your conscientious input.

Most of the questions that I wanted to ask have been asked. But I have a few technical ones which I would like to submit to you for your consideration and response.

I have just one, as a matter of curiosity, in following Senator Gore, on restriction on these traffickers.

What do you think about some provision that would require a purchaser to hold on to his operation for at least five years before he can sell it?

Mr. **Malone**. Well, I guess from my perspective, you would be better served to say that if he does sell it before five years, there is some large tax or he has to forfeit the gain, or something, because illiquidity would be a problem, I would think, with lenders and so on.

I don't think you'd want to stop people from buying properties, but I think you'd want to stop them from making profits, that is, short-term profits from trading in these things. That would be my reaction.

Senator **Inouye**. So you think we should provide a disincentive of some sort?

Mr. **Malone**. Correct.

Senator **Inouye**. Is that your view?

Mr. **Robbins**. Senator, I think philosophically, I do not disagree with where Mr. Malone is coming from. We are a long-term player in the business and operate on that basis.

So, philosophically, I am not opposed at all to some anti-trafficking provisions.

Mr. **Mooney**. It would be very difficult to argue against that, Senator, very difficult. I would not propose to do it.

Senator **Inouye**. As you noted, because of the importance of the panel before us, as Chairman of this subcommittee I did not impose any time restriction. As a result, we have been sitting here for close to three hours, because I know we are going to come out with some legislation. I want to make certain that what we do come forth with is a proper one.

I have been advised that Senator Gore has a few more questions.

Senator **Gore**. I know what a burden it is to ask a few more questions, given the time, Mr. Chairman. The only reason I impose on your courtesy is because we have not yet covered the question of satellite dish owners.

The satellite dish industry, in my opinion, has been crushed by the cable television and cable programming industry, and I think the legislation which is now obviously going to come out in this Congress has to deal with this question.

Mr. Malone, let me ask you this.

Do you think that the satellite dish owners are getting a raw deal where the decoders are concerned?

Mr. **Malone**. Unfortunately, I think so. Yes.

Senator GORE. How should we help them get some justice where the decoders are concerned?

Mr. MALONE. I really don't have an answer for you.

I have asked my people to think about what could be done, and I think we have asked our cable laboratories unit to take a look at the technology to see if there is some outside input to this dilemma that could perhaps eliminate the burden on the consumer and on everybody.

Senator GORE. Again, Mr. Chairman, I want to underscore the significance of this testimony for the record.

We have broken a lot of new ground here today, and you are one of the best witnesses that I have ever seen come before this Committee.

Senator INOUYE. So he is no longer Darth Vader?

Senator GORE. Isn't it true that some of your employees bought Darth Vader masks after that?

Mr. MALONE. That's right.

Senator GORE. He has made a number of acknowledgements here today. And here again, the problem with the decoders is one that we really have to deal with.

Now, I think also access to programming by satellite dish owners has to be dealt with.

We had testimony earlier, Mr. Chairman, that the only noncable distributor of satellite programming, the NRTC, set up after political pressure was applied to the cable industry—they finally said oh, we'll deal with the rural telephone folks—they said they are forced to pay 444 percent higher wholesale rates than cable operators pay for exactly the same services.

Let's take the example of TBS. Small cable operators pay 10 cents per customer per month for TBS.

Correct, roughly?

Mr. MALONE. [Nods affirmatively]

Senator GORE. You would probably pay less than that, wouldn't you?

Mr. MALONE. Right.

Senator GORE. What—two cents a month?

Mr. MALONE. Well, we own it, so we don't charge ourselves.

Senator GORE. Okay.

Why do the satellite dish owners, why does NRTC, to distribute it to satellite dish owners, have to pay not two cents a month, not 10 cents a month, but 90 cents per customer per month? Why is that fair?

Mr. MALONE. Do you mean at wholesale or at retail?

Senator GORE. Wholesale.

Mr. MALONE. I think that it is lower than that at wholesale. But I stand to be corrected.

Senator GORE. That's not what NRTC says.

Mr. MALONE. The first thing, the first differential, Senator—and I haven't had time really to explore that, but I certainly will, because we do have the information—the first difference that I can put my finger on is Copyright fees.

In other words, when we deliver it to a cable company, the cable company is responsible for the Copyright fee payment, which is about 12 cents, I believe, or whatever it is, based on that market.

When we deliver it to a home earth station indirectly, we pay the Copyright fee, and I think that is something in the neighborhood of 12 cents of the differential.

There are fairly extensive costs related to dealing with the individual customer on a channel, as opposed to the wholesale sale to cable. I'll summarize that very quickly.

In order to be in the retail business, a programmer has to make a deal with that addressability facility in California, which involves a one-time capital investment of about half a million dollars and ongoing costs of about $50,000 a month.

If you amortize that over the number of customers, you get something in and around the wholesale rates that are being charged to the earth station packagers.

Senator GORE. I think that is in the "Wizard of Oz" category rather than the "Darth Vader" category. That is kind of sleight of hand.

If you have a distribution technology, if you have a distributor that has to incur the capital costs of putting lines on poles and building a big distribution facility and spending all that money, and then you have another distributor where the customer makes the capital investment, instead of the distributor, it is not credible to say that the customer who makes the capital investment himself has to pay 444 percent more because it is more complicated to file the computer number in the file in order to keep track of the billing.

That's nonsense. With all due respect, that is just not going to wash.

Mr. Mooney, you said market penetration is one of the factors that we ought to look at.

You are buying Showtime, Mr. Malone.

What is the market penetration among all satellite dish owners for Showtime? Has it reached 5 percent yet?

Mr. MALONE. Well, I think I have a non-disclosure agreement with the information that I have on Showtime. And I am not supposed to talk about it. But I will estimate that the penetration, if you take all satellite dishes that have been sold, and divide that into how many customers Showtime has, you get about 9 percent.

Senator GORE. Okay, 9 percent economists would say is pretty good evidence of a non-competitive situation. But Showtime is the only distributor who has agreed to deal, that is, the only programmer who has agreed to deal with a non-cable distributor.

I am going to ask my staff to put up this other chart here that shows the difference. This is the only case that exists in the country.

They charge $76.80 a year for the cable distributor and 83.6 percent more to the non-cable distributor. How come? Why?

Mr. MOONEY. Oh, I think they are in the business of selling direct to the TVRO customer themselves. That is the business in which they function as a retailer, as well as a wholesaler. And I think, they think they have a position to protect in that respect as well.

Senator GORE. Well, yes. I mean, that is the whole point. The programmers that are owned by and/or controlled by the cable industry, have an interest in not allowing this new technology to compete effectively with cable.

That is why we have the 440 percent higher wholesale rates. And most importantly that is why we have an absolute and total refusal to sell to any distributor, to a satellite dish owner, who is not a cable television company.

Mr. MOONEY. Senator, you mistook what I said. They are themselves a retailer to the TVRO industry. Viacom, which is the company that owns Showtime thinks of itself as a programming company.

They are a programming company that owns a mid-sized cable distribution company as well. But they are primarily programmers and the psychology of that company is programming. The cable company does not wag the dog.

And for whatever their reasons, and I think it has to do with, who gets to keep the margin in the TVRO business, the decisions of Showtime and TVRO are not dictated by the interest——

Senator GORE. They are not dictated by the people who own them?

Mr. MOONEY. No, the cable company does not own them.

Senator GORE. Are you not buying Showtime, Mr. Malone?

Mr. MALONE. Well, actually, we had made an offer to invest in Showtime, but we have not bought them yet. Nor have they even signed a contract at this point.

Senator GORE. Let me just ask you a hypothetical uestion, Mr. Mooney.

If a programmer decides to sell its product to satellite dish owners, do you think there is anything wrong with the programmer establishing a policy that it will not sell to satellite dish owners, through any distributor who is not a cable television company?

Mr. MOONEY. I think that if the programmer had valid business reasons to do that, that would be acceptable. Having said that, I know, almost, none of them who have taken that position. Very few of them have taken that position.

Senator GORE. At equal terms and rates?

Mr. MOONEY. Well, you are asking me a different question.

Senator GORE. No. It is the same question with that proviso.

Mr. MOONEY. I think that if they decide that it is in their business interest to do that, that they will do that. I do think that most of them believe that the back yard dish market offers an opportunity for a better margin than the cable distribution market.

And they want to get that additional margin.

Senator GORE. I only have one other question. But I do want to underscore the significance of that one, Mr. Chairman.

If the cable television industry provides 95 percent of the money that comes into a programmer and the cable television industry says to the programmer, look, we want to distribute to any satellite dish owners. And we want to keep the price, above the price paid by our cable customers, then, the programmer is faced with enormous economic intimidation.

If the programmer does not comply with the wishes of the cable industry, they stand to lose access to their principal source of revenue.

The cable industry has an interest in preventing free access by the dish owners, because this is the new competition that can provide a price check on their prices just as Mr. Malone said, video tape rentals provide some degree of price check on paper view movies over cable now.

The cable industry does not want a price check of this sort from the dish owners. And, so, they intimidated the programmers to let them, the cable companies, control all distribution to the dish owners.

It is an outrageous situation. Now, there is a new technology, KU-band. Many people have been wondering when will the new, smaller dishes become available.

Then, the satellite dish industry may become even more common in America.

Mr. Malone, are you negotiating to buy up the KU-band capacity on the K-1 satellite owned by General Electric?

Mr. MALONE. Well, first of all, I disagree with some of your facts on the distribution prices and availability and the cable "stranglehold" on supply there.

If I can address that for a minute. I did look up, for instance, HBO. HBO offers cable operators nonexclusive rights to distribute HBO product in their own cable markets, only in their own cable markets.

And they price that, I believe, at $5.50 a month, which is the same price that they price to satellite packagers. TCI, which is far and away HBO's largest customer, buys HBO programming wholesale for, I think, $4.27.

HBO tells us that they have costs of dealing on a—so what you see is the difference between the largest customer and the very smallest and back-yard wholesaler, is a little over $1. And they maintain that that is entirely justified by the cost of handling the business.

So, to me, that is sort of more where it is. And right now at a retail level, a home earth station customer can buy essentially a basic package of cable programming from a number of packagers at or around $10 to $11.

The basic channels, which is about two-thirds of the average bill for basic cable, with that answer, I would say that, yes. We are and have been talking to GE about in some way or other providing us with some K-band capabilities, primarily aimed at high definition and paper view as a channel expansion capability for some of our systems in the industry. And also as an insurance policy in the event that high definition is something which our cable systems cannot handle.

But we are talking to them about only a portion of that one satellite. And I do not believe there is any effort here to preclude competition, or otherwise allow other people to play.

Senator GORE. Mr. Chairman, as you might expect, I could go on for some length responding to and debating with this panel the facts of the satellite dish situation.

I think it is well-documented. And I will provide additional material for the record to challenge some of the statements you have just made here. I think it is just completely outrageous. And where the K-1 satellite is concerned, please forgive me, if I feel a little bit cynical about some of the motivations that the cable industry might have for buying up the transponder capacity of the only KU-band satellite now available for television broadcasting.

I know that you want an insurance policy against several contingencies including a policy against the possibility that these smaller dishes might be a much more powerful source of competition for the cable industry.

But, again, you can disagree. And I respect each member of the panel. And I appreciate the time that you have given me, Mr. Chairman.

Thank you.

Senator INOUYE. Thank you.

I would like to thank you gentlemen for your patience and your contributions this morning. I can assure you that your contributions will be studied very carefully.

You have been very patient, thank you.

Mr. ROBBINS. Thank you, Mr. Chairman.

Mr. MALONE. Thank you.

Mr. MOONEY. Thank you.

Senator INOUYE. Our next panel consists of the Mayor of the City of Newark, the Honorabie Sharpe James; the Mayor of the City of Henderson, Tennessee, the Honorable Charles Edward Patterson; the Director of the Department of Commerce and Consumer Affairs of Hawaii, Mr. Robert Alm; Councilwoman City of Bayonne, Bayonne Municipal Center, New Jersey, Ms. Dorothy E. Harrington. And the Mayor of the City of Loredo, the Honorable Saul N. Ramirez.

I hope those who are leaving the hearing room will do so expeditiously. We have two more panels. May I first call upon the Mayor of the City of Newark, Mayor James.

STATEMENT OF SHARPE JAMES, MAYOR, CITY OF NEWARK, NJ

Mr. JAMES. Mr. Chairman, Senator Inouye, members of the subcommittee, on behalf of the National League of Cities and the United States Conference of Mayors, I thank you for the opportunity to testify here today.

The League represents more than 16,000 cities and towns and the Conference represents the 800 cities in the country with populations exceeding 30,000 residents.

Since cable television is increasingly becoming a major source of video information to most homes, issues involving this medium are of critical importance to our nation's municipalities.

When Congress passed the Cable Communications Policy Act of 1984, the Congress and the cities hoped the measure would foster technological innovation and competition. And, this in turn, would result in improved, yet affordable cable service for cable subscribers.

Unfortunately, as a result of unforeseen actions taken by the FCC, the courts and the cable industry itself, these goals have not been achieved. The Cable Act was designed to create a balance between the needs of the cable industry and the needs of the public.

However, it has failed. And, in fact, has created an imbalance in favor of the industry and at the great expense of the consumer.

Over 99 percent of the nation's cable systems do not face competition from another cable system.

The FCC has adopted regulations which make it impossible for cities to protect consumers from sky-rocketing cable rate increases. These regulations also preclude franchising authorities from insuring the cable operators provide a signal quality commensurate with developments in modern technology.

At the same time, the federal courts have narrowly construed the power of franchising authorities under the cable act. While the renewal provisions of the act have given cable operators claims to a perpetual monopoly and little incentive to upgrade service.

The result is that the cable industry has become a virtually unregulated monopoly which has not been fully responsive to consumer needs and interests.

In Newark, for example, I pay almost $70 a month for cable service from my local franchise Gateway Cable and this fee does not include every available option.

Basic service rates in Newark have, in fact, increased by more than 130 percent since FCC deregulation at the end of 1986. In addition, nearly half of our population still does not have cable service available to it.

Every day residents stop me in the street, or call my office complaining about the poor service from the local cable franchise. Without being able to offer an alternative to the current operator the city is often blamed for the poor quality, the poor coverage of service and rising costs.

As a councilman, I voted for the first cable TV franchise in the City of Newark and what we witnessed is, they hold it for one to two years, sell it twice the price, another company comes in and hold it for two to three years, sell it, double the cost. And who pays, is a fair question. That cost or the margin of the profit is passed on to the consumer.

If the American public is ever to receive the benefits envisioned by the cable act, Congress must pass legislation which permits cities to protect their constituent's interest and receive quality cable service at an affordable price.

The Conference and the League have adopted a series of resolutions identifying those cable issues which require prompt legislative attention.

We are pleased that several members of Congress, including members of this subcommittee have introduced bills which reflect some of the principles embodied in our cable television resolutions.

We look forward to working with the Congress in developing specific legislative recommendations, which will address all of the issues of concern to our constituents.

Mr. Chairman, I request that you keep the record open for a few weeks so that the League and Conference can submit their legislative recommendations along with a detailed analysis of the issues of concern to franchising authorities and cable consumers.

This will permit the League and the Conference to provide you with specific proposals, which are responsive to the matters raised at these hearings and which take an account of the principles set forth in both organizations' resolutions and recently introduced legislation.

In the meantime, I have included in my written testimony the League's and Conference's tentative conclusion on how best to resolve current regulatory and competitive problems in the cable industry.

The League and Conference strongly believe that cable legislation must among other things grant franchising authorities the power to insure that any rate increases are fair, reasonable and justifiable. And also to establish meaningful signal quality technical standards which are responsive to consumer needs.

Such legislation also should stimulate competition in local franchise areas by allowing franchising authorities to solicit additional bids to a franchise during a renewal process and by simplifying that process.

In addition, I hope that Congress will consider lifting under appropriate circumstances the federal ban on cross ownership of cable and telephone businesses, thereby providing potentially realistic options for those dissatisfied with current cable service.

Mr. Chairman, I wish to thank you again for this opportunity to share with you and the subcommittee our concerns in an area which has an increasingly profound effect on all Americans.

I trust that you will take the action necessary to enable a greater segment of our population to enjoy quality cable service at affordable cost.

Thank you for this opportunity to testify.

[The statement follows:]

TESTIMONY OF

THE HONORABLE SHARPE JAMES
MAYOR OF THE CITY OF NEWARK, NEW JERSEY
ON BEHALF OF THE NATIONAL LEAGUE OF CITIES
AND THE UNITED STATES CONFERENCE OF MAYORS

BEFORE THE UNITED STATES SENATE
COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION
SUBCOMMITTEE ON COMMUNICATIONS

November 16, 1989

Mr. Chairman, Members of the Subcommittee, on behalf of the National League of Cities ("League") and the United States Conference of Mayors ("Conference"), I thank you for the opportunity to testify today concerning the need for cable television legislation. As you may know, the League represents more than 16,000 cities and towns across the nation, and the Conference represents the more than 800 cities with populations exceeding 30,000 residents.

My testimony will focus on how changes in the cable television industry and actions by the courts and the Federal Communications Commission have undermined the objectives of the Cable Communications Policy Act of 1984. The nation's cities strongly believe that consumers will not realize the significant benefits contemplated by the Cable Act unless Congress takes prompt legislative action which restores local control over cable and opens the cable industry to meaningful competition.

I. NATURE OF MUNICIPALITIES' CONCERNS

Issues involving cable television are of critical importance to consumers and cities nationwide. Cable systems are currently franchised to serve some 85 percent of the approximately 90 million households in the U.S.; nearly 50 million of these households now subscribe to cable. See Cablevision, Sept. 11, 1989, at 80. Over 99 percent of the cable systems in this country do not face competition from another cable system; furthermore, alternative multichannel video programming distributors are not yet viable competitors to cable systems in most cities. Thus, the local cable operator is often a citizen's only multichannel video source of news, information and entertainment programming.

Cities had hoped that the 1984 Cable Act would foster competition and technological innovation in the cable industry and that it would promote improved, yet affordable, cable service for cable subscribers. Unfortunately, however, these goals have been undermined by the FCC, the courts and the cable industry itself.

The FCC has made it impossible for cities to protect consumers from skyrocketing cable rates. It also has refused to update its antiquated twenty-year old technical standards for cable signal quality, and has prevented franchising authorities from filling the void left by the absence of meaningful standards.

Furthermore, federal courts have narrowly construed the power of franchising authorities under the Cable Act and, in some decisions, have held that a municipality's exercise of such authority is unconstitutional. The interplay of deregulation and the Cable Act's renewal provisions (which help perpetuate an incumbent cable operator's monopoly power) have encouraged the cable industry to behave with the type of consumer disregard that one might expect from an unregulated monopolist.

The League and the Conference have adopted a series of resolutions (see Attachment) identifying those cable issues which warrant prompt legislative attention. The League and Conference are pleased that numerous Members of Congress, including Members of this Subcommittee, have introduced bills which reflect certain of the principles embodied in these resolutions. We look forward to working with the Congress in developing specific legislative recommendations which address all of the issues of concern to our constituents.

Mr. Chairman, I request that you keep the record open so that the League and Conference can submit their recommendations, along with a detailed analysis of the issues of concern to cities and cable consumers. This will permit the League and the Conference to provide you with specific proposals which are responsive to the matters raised at these hearings and which take account of the principles set forth in their resolutions and in recently introduced legislation. In the meantime, I would like briefly to discuss the problems that have arisen under the Cable Act, and to share with the Subcommittee the tentative conclusions of the League and Conference on how to resolve those problems.

II. CABLE ISSUES REQUIRING LEGISLATIVE ATTENTION

A. Rate Regulation

One of the most important cable issues confronting franchising authorities concerns the dramatic rate increases cable operators have imposed on consumers since passage of the Cable Act. Such increases threaten to divide this country into the haves and the have nots in terms of access to cable television. Since cable has become the bottleneck of video information into most American homes, cable operators often are able to take economic advantage of subscriber dependency on cable. FCC regulations have fueled the temptation of cable operators to do so.

When Congress passed the Cable Act, it directed the FCC to establish regulations which permit franchising authorities to regulate basic service rates where the cable operator in not subject to "effective competition." The cities hoped that the Commission would implement a realistic standard of "effective competition." Instead, the FCC defined the term in a manner which, pursuant to the Commission's marketplace dogma, left 97 percent of the nation's cable systems free from all rate regulation. See General Accounting Office, National Survey of Cable Television Rates and Services, at 4 (August, 1989).

The FCC concluded that a cable operator, which typically provides 20 or more channels of programming, faces "effective competition" whenever at least three over-the-air television broadcast signals are received in 100 percent of a cable community. This standard was vigorously opposed by the Department of Justice, franchising authorities and various public interest groups, but was nevertheless upheld by the courts as within the discretion of the Commission.

The August 1989 GAO study confirms the inappropriateness of the FCC's standard, and demonstrates that the absence of rate regulation allows cable operators to use their monopolistic powers to charge consumers unfairly for the provision of cable services. The study shows that cable operators have increased rates by 29 percent per subscriber for basic cable service between December 1, 1986 (when basic cable rates were deregulated) and October 1988. Those increases are approximately three times the increase in the Consumer Price Index during that same time period.

Further, 45 percent of the operators reported increases in excess of 30 percent and almost one-fifth reported increases of more than 50 percent. Such substantial rate hikes would not have been possible in a marketplace subject to true competition or rate regulation.

Because cable operators rarely face viable competition from other cable systems in their franchise area, the only constraint on prices under current law is a decrease in consumer demand. However, many cable subscribers have become dependent on cable as a source of information and entertainment; thus, absent congressional action, cable operators will continue to be able to impose substantial price increases before the loss of revenue from cable subscribers choosing to disconnect their cable service exceeds the increased and unjustifiable profits from such price adjustments.

In order to protect cable consumers from further substantial rate increases, an appropriate definition of the term "effective competition" should be set forth clearly in the Cable Act itself, and not left to FCC whim. Such definition should turn on the presence in the community of a viable multichannel competitor to the cable system. Furthermore, rate regulatory authority should not be confined to "basic services" alone, but should extend to all cable services and charges related to such services. The concept of "basic service" is becoming an anachronism as the distinctions between basic cable and pay cable are blurred with new marketing techniques.

In addition, even in those franchise areas where "effective competition exists," Congress should grant franchising authorities the right to: (1) require that cable operators and other multichannel programming distributors provide important local news and information on a "lifeline" service tier, and (2) to ensure that the rates and related charges for such lifeline services are reasonable. Such a lifeline service tier should include PEG access channels, local television broadcast stations, and any other local programming a franchising authority reasonably finds in the public interest. No consumer should be denied access to an essential core of programming because of prohibitively-high costs.

B. Technical Standards for Signal Quality

Although cable rates have increased, cable operators have not similarly improved the quality of services to consumers, thus making the rate increases especially unfair. Cities have found their ability to require cable operators to make commensurate improvements in cable service hampered by, among other things, FCC and judicial limits on their ability to adopt meaningful technical standards for cable signal quality.

Indeed, the FCC has never updated its nearly twenty-year old technical standards for Class I cable channels (those carrying over-the-air broadcast signals) to reflect developments in cable technology -- notwithstanding its repeated acknowledgment that these standards are "incomplete" and were intended only as a "first step" to defining adequate signal quality. At the same time, the FCC has prohibited cities from negotiating with their cable operators standards different than the FCC's. The Supreme Court has held that Congress intended in the 1984 Cable Act to codify this restrictive FCC preemption policy, even though there is absolutely no reference to the FCC policy anywhere in the Act or its legislative history. City of New York v. FCC, 108 S. Ct. 1637 (1988).

To date, the FCC has not adopted any signal quality standards whatsoever for the newer (non-Class I) channels of cable service (such as satellite-delivered channels, PEG and commercial access channels and two-way services); and it has prohibited franchising authorities from doing so. The U.S. Court of Appeals for the D.C. Circuit correctly held that such a prohibition in the absence of standards was arbitrary and capacious. However, in response to the Court's directive to consider adopting the necessary standards for non-Class I channels, the FCC has simply proposed to extend to those channels its twenty-year old Class I standards -- without making any effort to consider what changes should be made in these outmoded standards.

Section 626 of the Cable Act requires franchising authorities to consider the cable operator's "signal quality" in determining whether to renew that operator's franchise. Furthermore, franchising authorities are required to evaluate, on a day-to-day basis, the substantial number of subscriber complaints about signal quality. The complete absence of any meaningful signal quality standards at the federal level, combined with a prohibition on the adoption of such standards at the local level, have deprived franchising authorities of an objective basis for assessing whether a cable operator is in fact providing satisfactory signal quality.

In order to ensure that consumers receive adequate signal quality, Congress should require the FCC promptly to establish complete and updated technical standards for all cable services; these standards should define satisfactory levels of signal quality, which reflect developments in contemporary cable technology. Compliance with the standards should be enforced by the FCC and should, at their option, also be enforced by local franchising authorities. Furthermore, Congress should grant franchising authorities the independent right to negotiate with their cable operators technical standards for signal quality which differ from the FCC standards and which are suitable for the particular circumstances surrounding the local community.

C. Renewal of Franchises

Another major concern of franchising authorities involves renewal under Section 626 of the Cable Act. Only recently have courts, cities and cable companies grappled with the meaning of the Act's renewal provisions since the provisions did not apply to cable franchises expiring prior to mid-1987.

Section 626 is intended to balance the interests of cable operators and franchising authorities in the renewal process. In fact, however, the renewal provisions are procedurally and substantively complex and severely limit the power of franchising authorities. Furthermore, they compel franchising authorities to assume adversarial positions with cable operators to avoid waiving their rights and to prepare the documentation necessary to deny renewal. Most significantly, the provisions of the Act make it difficult for a franchising authority to deny renewal of a franchise to a cable operator that has not adequately served the community's needs.

Recent court decisions have further weakened the power of franchising authorities during renewal proceedings by imposing procedural burdens in addition to those already in Section 626. Such decisions are especially troubling for smaller cities and towns with scarce resources. Franchising authorities may find it difficult to review effectively a cable operator's renewal proposal if they are required to abide by the cumbersome renewal provisions and to litigate challenges to their renewal authority under the Cable Act.

As the law presently stands, many cable operators will not have an incentive to provide the full measure of quality cable service. A cable operator will assume that a franchising authority's threat not to renew a franchise, if services are not improved, is just that -- a threat, which a franchising authority may have little ability to enforce under the current renewal provisions.

In order to strengthen the ability of franchising authorities to deny renewal of franchises to cable operators providing inadequate cable service, Congress should eliminate the cumbersome procedural requirements in Section 626; franchising authorities should be permitted to structure renewal proceedings in any manner which they deem appropriate, as long as such structure accords with applicable law. Further, Congress should amend Section 626 to clarify that a franchising authority can consider a number of important factors as relevant to its renewal decision, such as a cable operator's ratemaking history; employment practices; character qualifications; ownership of other media interests; and any other public interest factors which a franchising authority reasonably deems relevant to its renewal decision.

Congress also should clarify that, even in circumstances where a renewal proposal satisfies all the statutory criteria, a franchising authority retains the right to deny renewal if the franchising authority and the cable operator fail to reach agreement on the material terms and conditions of the renewal agreement. As a means of introducing new competitive factors in the cable industry and encouraging cable operators to provide better service during a franchise term, Congress also should grant franchising authorities the right to solicit additional bids for the franchise during the renewal process; cities should be allowed to grant the franchise to a competing bidder if the bidder is better able to serve the community's cable television needs.

D. Horizontal and Vertical Integration

Cities are concerned that increasing horizontal concentration and vertical integration in the cable industry will make it difficult for independent cable companies, cable programmers and alternative multichannel video programming distributors to compete with multiple system operators ("MSOs") and their affiliated programmers. Despite the growth in the cable industry, MSOs have garnered an increasingly inordinate share of the cable market. In 1980, the five largest MSOs provided access to 29 percent of all cable subscribers; now those MSO's account for more than 40 percent of all subscribers.[1]

Large MSOs may use their substantial economic powers to force cable programmers to provide popular programming exclusively to them in those few areas where the MSOs' confront some competition; likewise, they may deny access on their cable systems to unaffiliated programming sources. One study, for example, demonstrated that Time Incorporated (now Time Warner), which owns HBO and Cinemax, is less likely to carry Showtime and The Movie Channel on its cable systems, which are owned by Viacom, another MSO; similarly, Viacom, which owns Showtime and The Movie Channel, is less likely to offer HBO and Cinemax on its cable systems.[2] In either case, it is the consumer who is denied program diversity.

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[1] Harris, "D.C. Puts the Heat on Cablers," Variety, April 13, 1989, at 1; Kriz, "Communications Focus," National Journal, April 29, 1989, at 1085.

[2] M. Salinger, "A Test of Successive Monopoly and Foreclosure Effects: Vertical Integration Between Cable Systems and Pay Services" (Sept. 1988).

Cable programmers affiliated with MSOs may refuse to sell, or sell only on unfavorable terms, programming to unaffiliated cable systems and other multichannel video programming distributors. For example, the Chief Executive Officer of the National Rural Telecommunications Cooperative ("NRTC") has testified that the 17-channel, basic service package that the NRTC offers to home satellite dish owners costs on the average 444 percent more at wholesale than a cable distributor would pay for the same 17 channels.[3]

Such conduct by MSOs and their affiliated programmers hamper the competitive goals of the Cable Act. If Congress does not take action, in a few years a small handful of MSOs and their affiliated programmers may totally dominate the programming choices of American consumers. The price consumers may pay for such dominance is a significant increase in cable rates and a corresponding decrease in the diversity of programming on cable systems.

In order to promote competition and limit horizontal concentration, Congress should put a cap on the number of the nation's cable subscribers an MSO and its affiliates can serve. Further, Congress should grant franchising authorities the right to deny ownership or control of a cable system because of a person's ownership or control of other media interests. Franchising authorities also should be permitted to take appropriate actions to alleviate such ownership concerns (e.g., requiring that a cable operator divest itself of other media interests as well as reducing and dividing a franchise area when granting, renewing or transferring a franchise.)

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[3] B. Phillips, Testimony Before the United States Senate Committee on Commerce, Science, and Transportation, Subcommittee on Communications (June 21, 1989).

In order to eliminate the negative effects of vertical integration, Congress should: (1) prohibit cable operators from discriminating against programmers unaffiliated with cable operators in the price, terms and conditions of access to their cable systems; and (2) prohibit cable programmers affiliated with cable operators from discriminating against unaffiliated cable operators and other multichannel programming distributors in the price, terms and availability of their programming. Violations of such anti-discrimination provisions should be remedied through civil actions brought by aggrieved parties. In such actions, after an aggrieved party establishes that it has been discriminated against, a defendant programmer or cable operator should bear the burden of persuasion in demonstrating a nondiscriminatory, pro-competitive reason for its actions.

As an additional means to ensure unaffiliated programmers access to cable systems, Congress should amend the current leased access provisions in Section 612 of the Cable Act so that: (a) cable operators are required to make publicly available a tariff specifying the rates, terms and conditions of leased access; and (b) franchising authorities have the right to approve such rates, terms and conditions.

E. Must-Carry and Retiering

Cities are concerned about the continued viability of local television broadcast stations, which have long been an important source of local news and information to consumers. Increasing vertical integration raises concern that cable companies will eliminate (or switch to undesirable channel positions) broadcast stations in favor of affiliated programmers. The exclusion of broadcast stations from cable systems will limit their access to home viewers, thus threatening their continued economic survival and the supply of important local programming to consumers.

These concerns result from the judicial elimination of the FCC's longstanding must-carry rules, which required cable operators to carry the signals of all local television stations within their service areas. The problem is compounded by Section 625(d) of the Act which allows cable operators to realign their service offerings if they are not subject to rate regulation. Realignments have made it difficult for cable subscribers to locate programming and have resulted in complaints to franchising authorities by programmers whose services have been retiered or shifted to a new dial location.

In order to ensure that consumers continue to receive programming of local interest presented by free local broadcast stations, Congress should condition a cable operator's right to carry television broadcast stations pursuant to the Copyright Act's "compulsory licensing" provisions upon its carriage of all local television broadcast stations (as required by the former FCC must-carry rules). Disputes over channel positioning of such stations should be resolved by franchising authorities pursuant to appropriate congressional guidance.

To ensure that low-income cable subscribers have access to broadcast programming, Congress also should require that local broadcast signals be offered as part of the tier of cable service regularly provided to all subscribers at the minimum charge. Further, so that cable consumers are not confused by a constant reshifting of programming, Congress should grant a local franchising authority the right to approve retiering decisions by local cable operators, regardless of whether the operators are subject to rate regulation.

F. Enforcement Provisions

Many franchise agreements contain penalty provisions applicable when cable operators breach the terms of such agreements. At least one court, however, has held that such provisions are unenforceable if a cable operator initiates a proceeding under Section 625 of the Cable Act to modify its franchise agreement.[4] Cities are concerned that this ruling will allow cable companies to stay liability for past franchise breaches simply by filing a Section 625 request for prospective modification of the franchise provision that the cable operator breached. Cities are also concerned that this decision might be construed, however improperly, to impair their right to enforce franchise provisions during renewal proceedings. The League and Conference do not believe Congress intended that cable operators misuse the Cable Act to prevent franchising authorities from enforcing franchise obligations to which companies agree, but later decide to ignore.

In order to clarify a franchising authority's right to enforce a franchise agreement, Congress should amend Sections 625 and 626 of the Cable Act, which govern modifications and renewals, to clarify that a franchising authority has the right to enforce the penalty provisions in a franchise agreement if a cable operator breaches the terms of the agreement -- regardless of whether the cable operator institutes a proceeding to modify the breached provision or to renew the franchise prior to, or subsequent to, such a breach.

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[4] Tribune-United Cable v. Montgomery County, 784 F.2d 1227 (4th Cir. 1986).

G. Franchise Fees

Section 622 of the Cable Act clearly permits franchising authorities to impose on cable operators a franchise fee of up to five percent of that operator's gross annual revenue. However, Section 622 does not clearly identify those assessments which are or are not included in calculating the five percent franchise fee cap. In addition, one cable operator has successfully challenged on constitutional grounds a city's right to collect franchise fees in accordance with the Cable Act.[5] Other courts have restricted the right of franchising authorities to collect fees which clearly should not be subject to the five percent franchise fee cap.[6] Another area of uncertainty concerns the extent that states can prohibit municipal franchising authorities from collecting franchise fees to the full extent allowed under the Cable Act.

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[5] See Century Federal, Inc. v. City of Palo Alto, 710 F. Supp. 1559 EFL (N.D. Cal. 1988) (the court held that the defendant cities violated the First and Fourteenth Amendments by requiring the plaintiff cable operator to: (1) pay a franchise fee of five percent of its gross receipts; (2) post construction and performance bonds; and (3) establish a security fund).

Congress should amend Section 622 of the Cable Act to clarify that: (1) the term "franchise fee" does not include consultants' fees or attorneys' fees incurred in the awarding, enforcing, renewing, renegotiation, modification, amending, or transfer of the franchise; (2) no assessment, fee, tax, charges or in-kind payments assessed by a franchising authority should be considered a franchise fee unless such assessment is clearly and unambiguously defined as a franchise fee by a franchising authority; and (3) States are prohibited from barring local franchising authorities from collecting franchise fees to the full extent allowed under the Cable Act.

H. Damages Immunity

Increasingly, cities are finding their authority to regulate cable television systems challenged in court on various statutory and constitutional grounds. These lawsuits are expensive for cities to litigate and expose them to the possibility of extraordinary monetary judgments. As a result, the temptation is for cities to settle, rather than to defend, their authority in such suits.

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[6] See, e.g., Birmingham Cable Communications v. City of Birmingham, No. CV 87-L-0755-S (N.D. Ala. May 3, 1989) (judge's summary judgment order invalidated a city ordinance which would have required the cable company to pay the city's consulting fees accrued during the franchise renewal period).

For example, the communities of Palo Alto and Atherton, California, recently agreed to pay a cable operator $2 million to settle a lawsuit in which the court ruled that the cities could not collect franchise fees in excess of those imposed on comparable users of the cities' rights-of-way, even though such fees did not exceed the Cable Act's five percent cap. The cities stated that they needed to settle the suit in order to protect their taxpayers from an estimated $1 million appeal and a possible $10-$15 million damage assessment should they lose an appeal.

In order to protect franchising authorities which exercise their regulatory power pursuant to the Cable Act, Congress should immunize franchising authorities from damages in lawsuits that challenge cable television regulation and franchising on civil rights (Section 1983, First Amendment or Fourteenth Amendment) or any other grounds, unless the aggrieved party alleges that a franchising authority discriminated on the basis of race, color, sex, age, religion, national origin, or handicap.

I. Preemption

Congress intended for the Cable Act to "clarif[y] the current system of local, state, and Federal regulation of cable television." H.R. Rep. No. 934, 98th Cong., 2d Sess. 19 (1984) U.S. Code Cong. & Admin. News 1984, p. 4655. However, the Act does not clearly set forth the limits of all regulatory authority. As a result, the FCC has attempted to use jurisdictional ambiguities in the Cable Act to usurp local authority over some cable regulatory matters.

The FCC's successful preemption of local authority over technical standards for signal quality represents one example of the FCC taking advantage of such ambiguities in the Cable Act to the detriment of franchising authorities. Although courts upheld the FCC's prohibition on local regulation of technical standards, they candidly recognized that such preemptive authority is not clearly defined in the Cable Act or in the Act's legislative history. City of New York v. FCC, 814 F.2d 720 (D.C. Cir. 1987), aff'd, 108 S. Ct. 1637 (1988). Indeed, one judge noted in dissent that the majority's decision violated a fundamental principle of federalism that preemption is appropriate only where there is a clear manifestation of congressional intent sanctioning such preemption. See 814 F.2d at 728 (Mikva, J., concurring and dissenting)(citing

Schwartz v. Texas, 344 U.S. 199, 202-03, 73 S. Ct. 232, 234-35 (1952)).

In order to clarify the right of cities to regulate cable systems, Congress should prohibit federal and state agencies from preempting local cable television ordinances and the provisions of franchise agreements unless such preemption authority is expressly and unambiguously set forth in the Cable Act.

J. Transfers

There are few legal restrictions on the ability of a franchising authority to approve, disapprove, condition, or otherwise regulate the transfer of a cable system within its jurisdiction. The Cable Act is silent as to the role which cities may play in the transfer process. Thus, it is reasonable to assume that Congress intended that cities would continue to regulate transfers as they have traditionally done -- through the franchise process.

However, recent actions by Paramount Communications Inc. ("Paramount") raise questions about the extent of local franchising authority over transfers. Paramount requested the FCC to approve the transfer of control of Time, which holds numerous cable franchises, to Paramount.[7] The United States Conference of Mayors requested that the FCC not take any steps which would undermine or impair the legal rights of local governments to maintain their authority to approve all transfers of cable television franchises and transfers of control of cable franchisees.[8] The issue became moot (this time) since Paramount failed in its efforts to prevent Time from merging with Warner Communications Inc.

Because of the nature of the transfer process -- the importance of timing and the existence of possible hostile takeovers -- Congress should clarify that local franchising authorities have the right to approve or to disapprove cable system transfers pursuant to applicable state and local laws and to the terms of a franchise agreement. Congress also should add a statutory provision which clarifies that, in the absence of applicable laws and of provisions in a franchise agreement, franchising authorities have the right to deny a cable system transfer based upon: (a) past failure by the franchisee to comply with the franchise;

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[7] In Re Applications of: KDS Acquisition Corp. For Commission Consent to Transfer of Control of Time Inc., FCC File Nos. CAR-30727-09 through CAR 30825-09; 1579-SSA-TC-89 (95) et al. (June 9, 1989).

[8] Letter from J. Thomas Cochran, Executive Director of the United States Conference of Mayors, to The Honorable Dennis R. Patrick, Chairman of the FCC (June 21, 1989).

(b) a refusal by the transferee to agree to comply with the terms of the franchise in the future; (c) economic non-viability (as reflected in the purchase price and the economic impact of these acquisition costs on the community); (d) the length of time the cable system has been owned by the transferor and the extent of improvements made to the cable system during the transferor's ownership; or (e) any other technical, legal or character qualifications a franchising authority reasonably deems relevant to its transfer decision.

K. Public, Educational and Governmental Access Channels

Section 612 of the Cable Act grants cities broad authority to designate channel capacity on cable systems for public, educational, and governmental ("PEG") use and to enforce requirements for services, facilities and equipment for such use. Despite such broad authority, cities have been hampered in their efforts to require that cable operators provide adequate support to satisfy their PEG access obligations under a franchise agreement. Cable operators have, in fact, often ignored PEG access obligations which would require them to incur expenses in addition to a five percent franchise fee, thereby making it difficult for cities to maintain adequate PEG access facilities and to provide quality PEG programming for their constituents.

In order to enable franchising authorities to provide cable consumers the quality of PEG access programming and facilities they deserve, Congress should amend Section 622 to exclude from the "franchise fee" definition any expenditure, grant or in-kind payment by cable operators which are related to the use and operation of PEG access channels.

L. Telephone Company Cross-Ownership

Since the acquisition and start-up costs of cable systems are substantial, there are few potential competitors which have the financial capacity to enter and compete in the cable marketplace. Of the potential competitors, telephone companies ("telcos") are most often suggested as the best possible source of competition. In addition to providing competition in the provision of cable service, proponents of telco entry argue that telco entry also may result in technological innovation, such as the introduction of fiber optics technology, and cable service to areas which are not economically feasible for cable operators to serve.

The Cable Act, however, prohibits telcos from providing video programming to subscribers in their telephone service area (except in certain limited circumstances involving rural areas). Congress should reconsider this prohibition. If telco entry is desirable, Congress should give local franchising authorities the right to grant a cable franchise to a telco for the provision of cable television service and to impose on the telco the same franchising requirements imposed on other cable operators, including the imposition of franchise fees, so long as: (a) the telco sets up a separate subsidiary for its cable operations in order to prevent cross-subsidization; and (b) the telco is prohibited from acquiring an existing cable system unless authorized to do so by the local franchising authority.

If a telco's cable system is integrated into its telephone service, Congress should grant a franchising authority the right to impose through the franchise process: (a) consumer protection and customer service requirements; (b) PEG access requirements; (c) minimum requirements for cable system facilities and equipment; (d) franchise fees; and (e) any other franchising requirements deemed appropriate by a franchising authority. Further, such telcos should: (a) provide access to unaffiliated multichannel video service providers and programmers at nondiscriminatory tariffed rates; (b) offer switching and related service on a tariffed and unbundled basis; (c) not discriminate in favor of their own service offerings; and (d) expand and upgrade their facilities as demand increases.

III. CONCLUSION

Unforeseen developments since enactment of the Cable Act have hampered the effective local regulatory oversight of cable systems and have stifled competition in the provision of cable services. As a result, consumers have not received the benefits intended by the 1984 Cable Act. If such benefits are to be attained, Congress should enact corrective legislation consistent with the recommendations set forth above.

Senator INOUYE. I thank you very much, Mayor James. In response to your request the record will be kept open until January 15, 1990.

Mr. JAMES. Thank you.

Senator INOUYE. I will now call upon Mayor Patterson.

STATEMENT OF EDDY PATTERSON, MAYOR, CITY OF HENDERSON, TN

Mr. PATTERSON. Thank you, Mr. Chairman.

I appreciate the committee having these hearings on cable regulation. I am the mayor of Henderson, Tennessee. And I am especially pleased, that my own senator, Senator Al Gore, has taken the leadership role in helping us solve the issues of cable television.

We have a terrible cable situation in West Tennessee that simply will not fix itself. We need help from Congress to correct these problems created by the 1984 cable act.

I know that the committee has heard from some of the big cities on these issues. And I am pleased that I can now tell you how so many small communities are also suffering under these cable monopolies.

Henderson, Tennessee is located approximately half-way between Memphis and Nashville, Tennessee. Our television reception from an antenna source is very poor. People need basic cable television, as they did the automobile several years ago.

In fact, it is about the only form of entertainment that some of our senior citizens have in this area of West Tennessee. For many years a small multi-system operator Essex provided a good service at affordable rates.

Up until early 1988 we were receiving 17 basic channels of service for the price of $14.95. Shortly after Essex was purchased in mid-1988 by a cable group called Multivision, our local cable rates increased by about 40 percent, and with absolutely no additional channels or improvements to service.

I immediately began trying to contact officials of Multivision to request that they reduce their cable rates. But it became obvious that they had no intention of responding to local concerns.

After numerous complaints from the citizens of Henderson, Tennessee, we have been getting intensive investigation into the operations and cost of cable television systems. I contacted numerous suppliers, contractors, engineers, cable operators, to gather more information concerning this matter.

After a lot of research the city council decided to ask Multivision what they would ask to sell their Henderson system to the City of Henderson. I was quoted a selling price of $3.7 million.

But we had determined through investigation that we could actually build a totally better system to serve our residents of the City of Henderson for only about the cost of $1 million.

It was obvious that the price Multivision paid for the Henderson system alone was extremely inflated. And it was obvious who was going to pay for this speculation—our citizenry of Henderson.

I joined with several other mayors in West Tennessee whose towns are also served by this company and we collectively asked Multivision to reduce their rates as a group. But all we got was the cold shoulder. And, in fact, Multivision practically refused to discuss our concerns.

Several meetings were held in West Tennessee concerning cable television and regulation. Senator Al Gore conducted a workshop for the region to help us how to deal with Multivision's arrogance, and to get more information on how to enter the cable television business ourselves.

We contacted the FCC to find out what we could legally require of Multivision. Of course, we found out that our hands were tied. We went so far as to introduce and pass a private act in the Tennessee state legislature, which would allow the City of Henderson to construct and operate a cable television system.

In May of this year the Henderson Board of Alderman awarded a second cable franchise to another company called CableAmerica. This committee will be interested to know that just before the Board voted to invite competition in to compete with Multivision, representatives from Multivision handed me a letter, which essentially said it would lower rates but only if we did not allow another operator to come into the City of Henderson. I have included this letter with my testimony for your information which is attached to the testimony.

On November 3, 1989, CableAmerica began installing their first customers' hook-ups. Multivision immediately began cutting their rates. All of a sudden Henderson, Tennessee is enjoying the cheapest cable rates probably in America today. Remember that Multivision is the same company that only a year ago refused to even consider reducing their cable rates.

They are now offering free service for the next three months. I hope that the Senate now understands the frustration that the 22 West Tennessee communities have had with their cable operations. And I believe that this is happening to some degree all across the United States of America.

Deregulation serves some usefulness in some areas but in the cable television business it has created mostly monopolies. Companies pay the ridiculous price for some existing cable companies and have raised cable rates to unrealistic amounts in order to cover their investments.

I do not think I am against any one company making a profit, but to ask the customer to pay for a lot of blue sky and then guarantee the company a profit, because it made a stupid purchase is ridiculous.

I believe the only way the public can be served and served fairly is to do two things.

Mr. Chairman, I believe we need to return deregulation of local cable operations to the franchising authority. We do not want to make cable operators lose money, or tell them which programs they can and cannot show on television. But we do want to be able to represent our constituent's concerns about the run-away rates and poor service.

Secondly, we need to inject some competition into this situation by letting the cities invite in under regulation the telephone companies to also build cable systems. Obviously, you need to make sure the telephone companies cannot subsidize cable service with regulated telephone customer's money.

But, surely, this committee can figure out a way to prevent that. I believe Senator Gore's bill is the right approach, and I hope this committee and the Senate will pass it as soon as possible.

I certainly appreciate the opportunity to testify before this committee on behalf of all of the city officials who are trying to protect their interest of cable customers throughout the country.

Mr. Chairman, I have here with me some letters from the other mayors in West Tennessee and I ask that they be included as part of the record.

Thank you, Mr. Chairman.

Senator **Inouye**. It is so ordered.

I thank you very much, Mayor Patterson. I think you just got reelected.

Mr. **Patterson**. Thank you, sir.

[The following information was subsequently received for the record:]

OVERSIGHT OF THE 1984 CABLE ACT

POST HEARING QUESTIONS

BY: MAYOR CHARLES E. PATTERSON
HENDERSON, TENNESSEE

IN RESPONSE TO CONCERNS OVER RATE INCREASES, THE CABLE INDUSTRY HAS POINTED OUT THAT THE RATE INCREASES HAVE BEEN ACCOMPANIED BY AN INCREASE IN THE NUMBER OF PROGRAM SERVICES AND THAT THE COST TO THE SUBSCRIBER FOR EACH PROGRAM SERVICE HAS ONLY INCREASED BY AN AVERAGE OF ONE PENNY. WHAT IS YOUR RESPONSE TO THESE CONTENTIONS ?

I only have first hand information concerning our local cable situation. Multivision raised cable rates from $ 14.95 to $ 19.95 without providing additional program service. By there own admission, their cost of providing the 17 channel basic service was only $ 1.50 per subscriber. Based on the 1250 basic subscribers they had in the Henderson system, Multivision gross income after programming costs, excluding pay channels was $ 276,750.00 per year on a very small system compared to TCI or Cox Cable. As stated in the hearings by Mr. Malone and Mr Robbins, cable is a cash alligator business. That's true. The cable companies, especially where a monopoly exist, are gobbling up all the cash they can from the general public.

Competition was the only thing that has brought about more programming and a reduction in basic cable rates here in Henderson, we are luckier than most municipalities in that we were able to attract another company to overbuild the present cable company.

Rate increases with most programming services will no doubt go up as indicated in the litature I am enclosing for your information. But a 20% hike in the cost of programming when that cost is only twenty cents ($ 0.20) does not justify a 40% rate hike on the retail side. As you can see from the litature I have enclosed, small cable companies are charged at a higher rate than the large cable operators.

IF WE WERE TO FLAT FEE FOR BASIC CABLE OR "LIFELINE" SERVICE, WHAT PROGRAM SERVICES SHOULD BE INCLUDED IN THAT BASIC TIER AND WHAT SHOULD THE PRICE BE ?

I think most cable operators could provide a line up of 11 basic channels including all the local network affiliates for a fee between $ 8.00 and $ 10.00 a month and still make a hefty profit.

WHAT OTHER CHANGES DO IN THE RENEWAL PROVISION DO YOU FEEL ARE NECESSARY ?

I feel that the franchising authority and regulation should be with the local governments because circumstances are so varied from one location to another that only local authories have the first hand information to make a rational decision. I think it would be almost impossible to have federal regulations imposed on everyone and achieve equality for all.

Effective competition should be redefined to mean a second franchise from a competing cable company or the telephone companies. That in my opinion, based on our experience, would constitute effective competition.

YOU SUPPORT ELIMINATION OF THE RESTRICTION ON TELEPHONE OWNERSHIP OF CABLE SYSTEMS. HOW WILL THIS ENHANCE COMPETITION SINCE UNDER MOST ESTIMATES, THE BROADBAND NETWORK WILL NOT BE OPERATIONAL FOR DECADES ?

I support the elimination of restrictions on the telephone companies only where no other competition exists. In our own particular case, we have two cable companies therefore, eliminating the need for ownership by a telephone company.

In my conversation with telephone executives, it is my understanding that they can already provide cable service. The only thing holding them back are the restrictions placed on them.

DO YOUR FRANCHISE AGREEMENTS REQUIRE THE PROVISON OF PUBLIC ACCESS CHANNELS ?

Our franchise agreement with the second cable operator does have a clause requiring the provision for public access channels. Our agreement with the original cable operator does not include this provision.

HAVE YOUR CITIES ENCOUNTERED ANY DIFFICULTIES WITH CONTROVERSIAL OR OFFENSIVE PROGRAMMING CARRIED ON YOUR PUBLIC ACCESS CHANNELS ?

None, because we have not had this sevice before now.

Senator **Inouye**. A few years ago I had the good fortune to have on my staff a senior legislative assistant, the next witness. Today he serves as the Director of the Department of Commerce and Consumer Affairs for the State of Hawaii. So it gives me special pleasure to call my former assistant, Mr. Alm, to testify.

STATEMENT OF ROBERT A. ALM, DIRECTOR, DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS, HONOLULU, HI

Mr. **Alm**. Thank you, Mr. Chairman and Senator Gore.

The State of Hawaii is here to ask for the authority to again regulate cable television rates. Our State law in this area has always called for a careful balancing of the interests of cable operators and those of the public, and it has served us well.

In the 16 years prior to deregulation, Hawaii's systems enjoyed reasonable profits and a statewide penetration rate in excess of 70 percent, while 99 percent of Hawaii's residents were able to receive the best available cable technology.

Rate deregulation in 1986 upset this balance. Since then, cable rates have risen geometrically for most of Hawaii's consumers and most of Hawaii's systems have been sold to large multiple-system operators. For consumers living in systems which have been churned, sold two or three times in the last three or four years, rates have risen as much as 99 percent.

In the absence of rate regulation, systems have been bought and sold with seemingly little regard for the mounting levels of debt. In addition to the upward pressure on rates this causes, the increase in debt service requirements diverts funds from the current obligations to the communities that they serve. Hostile takeovers and, therefore, more debt are also possible outcomes in this environment.

This is not a healthy state of affairs for the consumers of Hawaii or the consumers of this Nation. In addition, price hikes and other policy decisions made by absentee MSO management drives a wedge between local cable operators and the communities they serve, as local managers are less and less able to be responsive to local concerns.

Rate deregulation has also dramatically increased cable system profits. In a recent franchise renewal, the State of Hawaii took great pains to assure that we did not create upward pressure on rates. Guided by a Price, Waterhouse study, the State imposed requirements which greatly enhanced the quality of the system but which also allowed the operator, Oceanic Cable, an ATC subsidiary and the tenth-largest system in the country, to meet the financial goals that they had stated in their own renewal application.

The system raised its rates anyway, citing an increase in its parent's profit requirements, and as a result in the third quarter of this year Oceanic is making an astronomical 27 percent after-tax profit.

That means that of each $17.95 monthly charge for basic service, nearly $5 is pure profit. And if you look on a consolidated tax basis Oceanic's parent, ATC, may well be receiving $8 a month in pure profit from every basic cable subscriber in Honolulu. That is simply not right.

These dramatic increases in rates and profits and the churning of cable systems are all merely indications to us that the competition anticipated at the time of the passage of the Cable Act has failed to materialize. Neither the direct competition of overlaying cable systems nor the competition of alternative technologies has occurred. And, as we see it, they are unlikely to do so in the near future.

In addition, off-air broadcast signals, given Hawaii's volcanic topography and many highrise buildings, simply fails to offer an alternative to many of Hawaii's residents.

Competition was the primary basis for rate deregulation, and it does not exist. And none of the arguments offered by the MSOs to justify their continued rate increases or to justify the trafficking of their systems are persuasive. MSOs which claim they are making up for the losses of the past are in fact claiming as their own the losses of the mom and pop entrepreneurs whose systems they have bought.

MSOs complaining about rising program costs would be better to talk to their affiliated programming companies. Systems comparing their rates to national rates or other locales miss the point. Rates must simply reflect local costs and local conditions.

Instead of suggesting that declining pay revenues be supported by increasing basic rates, systems ought to be looking for new sources of revenue. And arguments that stiff access or engineering requirements leave systems no choice but to raise rates are hollow in the face of astronomical profits.

Hawaii would respectfully request that rate regulatory authority be returned to State and local governments. These governments already successfully regulate in complex areas such as power, transportation and telecommunications, and this type of utility regulation can serve as a model, whether cable follows that exact route or not.

Hawaii would certainly not object to the return of rate regulatory authority, coupled with explicit Federal standards which promote equity for the consumer and a fair—and I underline that word "fair"—return to the cable operator. What we are therefore asking for is not a return to the good or bad old days, depending on your point of view, but, rather, a grant of rate authority coupled with standards to ensure the proper exercise of that authority.

This authority we must, however, have because only with a return to rate regulation can consumer protection again become a meaningful concept in the cable television field.

I thank you, Mr. Chairman.

[The statement of follows:]

STATEMENT OF ROBERT A. ALM, DIRECTOR, HAWAII STATE DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS 1/

MR. CHAIRMAN, MEMBERS OF THE COMMUNICATIONS SUBCOMMITTEE:

Mr. Chairman and Members of the Committee, thank you for letting me share the views of the State of Hawaii about the Cable Communications Policy Act of 1989 (hereinafter "1984 Cable Act"). While we have concerns about a number of features of the 1984 Cable Act, we will limit our testimony today to the need for cable rate re-regulation.

I. BEFORE THE 1984 CABLE ACT WENT INTO FULL EFFECT, HAWAII'S CABLE INDUSTRY AND CONSUMERS ENJOYED 16 YEARS OF BALANCED RATE REGULATION AT THE STATE LEVEL.

As one of a handful of jurisdictions to regulate cable television at the state level, Hawaii set out in 1970 to ensure that regulation would be uniform throughout Hawaii's six major islands. Our first regulators were particularly careful to allow for sufficient profitability

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1/ The exhibits were not reproducible.

to stimulate investment in new technology while at the same time keeping rates low enough to promote expansion of the subscriber base.

As a result of this balanced approach to rate regulation, Hawaii became one of the first states to be 99% cabled with many areas reaching 70% penetration and one large community attaining a penetration of 93%. Operators were rewarded in ratemaking for successfully installing new technology and as a result Hawaii became among the first to enjoy the benefits of microwave technology, addressable converter boxes, pay-per-view, time-delay transmission, and more recently, fiber backbone application. The aim throughout these years was to balance the operator's need for profit against the goal of making the best cable technology available to the widest possible population base.

II. SINCE DEREGULATION CABLE RATES HAVE RISEN GEOMETRICALLY --UPSETTING THE BALANCE THAT HAD EXISTED FOR YEARS AND DOING VIOLENCE TO THE PUBLIC INTEREST.

In the five years since 1984, Hawaii's cable systems have raised rates by as much as 99%, making Hawaii no exception to the national trend. The pattern is clear. Systems which have been churned have raised rates the most--presumably to cover the mounting debt associated with each successive buy-out. Those systems which are in the midst of a franchise renewal or transfer proceeding seem to delay their major rate increases until after they obtain the desired franchise, and then they raise rates with alacrity. Rate histories for Hawaii's cable systems are shown at Exhibit A. To highlight a few:

1. Sun Cablevision, sold twice in the last three years (Daniels, United Artists/TCI), has raised rates by 91% since 1984.
2. Chronicle Cablevision, sold three times in the last four years (McCaw, Cooke, Chronicle), has raised rates by 99% since 1984.
3. Kauai Cable has raised rates the least, by only 18%, since 1984. But this system has been under negotiation for sale for almost three years now.

Hawaii's largest cable system, Oceanic Cablevision serving 206,000 subscribers, has raised rates by 57% since 1984. The lion's share of this increase, 38%, came in the last year and a half when its parent, Time Inc., was seeking to market the cash flow of its cable entities during merger negotiations with Warner Communications. This merger was completed earlier this year, and now it appears that a great portion of the $11 billion in debt will be passed on to cable subscribers through purchase of the Warner cable subsidiary by Time's cable entity, ATC. Without rate protections, it now appears more dramatically than ever before that Hawaii's consumers will be asked to foot the bill of transactions that take place far from its shores.

The most glaring deficiency left in the wake of the 1984 Cable Act--in the area of rates--is that no one is able to help the consumers and the consumers are not able to help themselves. At the height of Oceanic's two large rate increases earlier this year, hundreds of complaints came flooding into the State's cable office each month. What is noteworthy about this is that before these rate increases went into effect, the State cable office rarely received more than forty or fifty complaints a year. In a state whose citizens for various reasons do not normally complain a great deal, Hawaii's consumers have apparently gone past the breaking point on cable rates. If further large increases are in the offing, and we understand this may be the case, we fear that the balance so carefully nurtured by the State of Hawaii for 16 years may never be restored as Hawaii's consumers suffer from what can only be viewed as corporate greed at its worst.

The 1984 Cable Act also does great violence to the delicate relationship between the local system management and the State. Our local system managers are all, except for Kauai Cable, answerable to multiple system operators ("MSO's") here on the mainland. The large MSO's are far removed from the problems of the local system manager in Hawaii, and yet more and more they are making decisions according to pressures not easily explained or accepted in Hawaii. Our local system managers inherit the negative ramifications of these decisions and must somehow suffer through the ire invoked in the communities in which they live. Along with this, the State suffers. Trying in vain to cajole and coax the local system manager into more reasonable rates and better community relations, the government's chief point of contact finds itself farther and farther removed from the accessibility to system decision-making and long range planning it once enjoyed. Here, too, it may be years before close planning ties and relations can be restored to what they once were.

III. SOME OF OUR CABLE SYSTEMS ARE NOW PRODUCING ASTRONOMICAL PROFITS WHICH ARGUES FORCEFULLY THAT RATES MUST IN SOME INSTANCES BE ROLLED BACK.

While local cable systems are being asked to pay off the debt acquired in the sale of multiple system aggregates, it is clear that the MSO's are not losers. After tax profits for Hawaii's largest cable system, Oceanic Cablevision, increased from 10% of revenues in 1984 to 27% of revenues in the third quarter of 1989. A profit margin of 27% is by any standard very high, and for Oceanic's parent company this figure is a godsend.

It is even more interesting to contemplate the value of this kind of profitability in a consolidated return. In this case, Oceanic's gross profit (profits before taxes) is reported directly to its parent ATC, and thence, to Time Warner Inc. These profits are stated against losses in other divisions. The net result may be no tax at all on Oceanic's gross profit. This means that Oceanic's gross profit before taxes (44.6% in the latest quarter) may be the MSO's true take from the local community.

To the Hawaii consumer, this means that 44.6% of every basic monthly cable service bill is potentially profit. In monthly terms, this translates to $8.00 out of every $17.95 going to the New York based parent. If nearly one-half of every consumer's dollar goes to profit, something is wrong. But even if "only" 27% is profit, that still means that $4.85 out of every subscriber's monthly charge for basic service is going to the New York parent.

The profit histories of the only two Hawaii cable systems which are corporations and not limited partnerships are shown at Exhibit B. The reason for these exorbitant profits appears to be something the 1984 Cable Act did not anticipate--the absence of competition.

IV. THE REASON RATE REGULATION IS SO DESPERATELY NEEDED TODAY IS THAT ALL SOURCES OF COMPETITION PRESUMED UNDER THE 1984 CABLE ACT HAVE FAILED TO MATERIALIZE.

The hope that competition would develop from two overlaying cable systems in one community has proven illusory. The prospect of designing and constructing two parallel cable systems is now seen to be cost prohibitive. And even if institutional financing could be obtained to build a second layer of capital intensive plant in every community, the reality is that there just isn't space on existing telephone poles or in existing ducts to accommodate a second system.

The establishment of a presumption in favor of franchise renewal for the existing franchise holder by the 1984 Cable Act, together with placing the burden of proof for non-renewal on the regulator, resulted in a further barrier to entry for the second cable operator. Consequently, although non-exclusive cable franchises have been mandated by law in Hawaii, the realities of cost, financing, limited pole space, and presumption of renewal all combine to create natural monopolies for existing cable systems in Hawaii.

Competition from direct air broadcast television has likewise proven illusory. In Hawaii, volcanic mountains and ridges have made it impossible to receive direct broadcast signals in such densely populated areas as Manoa, Palolo, Niu Valley, Hawaii Kai, Waianae, Haleiwa, and Kaneohe. FCC determinations of adequate signal quality have left the promise of direct broadcast competition unfulfilled. Of greater relevance, the federal standards for "effective competition" have failed to provide any relief by refusing to take into account whether quality signal is uniformly available. As a result, two residents living side-by-side on Manoa Road will have widely differing success at receiving quality signal from local broadcasters.

Homeowners in densely populated condominium communities like Makiki and Waikiki likewise experience problems but of a different variety. These homeowners complain of inadequate signal not because of volcanic ridges but because of "ghosting" caused by neighboring condominium structures. Thus, in Hawaii there are residents in different kinds of communities who are not adequately served by broadcast signals, even though under FCC standards these signals may be "theoretically" available to them. Competition from broadcast signals is therefore too spotty and too theoretical to be meaningful for many of Hawaii's citizens.

At the time of passage of the 1984 Cable Act, many believed that competition would be forthcoming from such alternative technologies as multiple distribution services (MDS), wireless cable services, and satellite reception dishes. These technologies are in existence today and are available to many communities. However, they suffer from enormously poor acceptance due to technologically limited channel capacity or to stiff restrictions on popular programming. In Hawaii, for example, if a competitor wanted to offer HBO in an area already being served by an established cable system, it would not be allowed to do so. ATC's "exclusivity rule" prevents the distribution of HBO through more than one distributor in any given community. Since HBO is the most popular pay channel, the prospects for a competitor's long term survival would be bleak even if basic services were offered at rock bottom prices.

With none of the anticipated sources of competition coming into fruition, it seems that the only recourse is for Congress to bring back rate regulation. The alternative is to perpetuate the current imbalance in cable rates and profits.

V. IN ONE GRAPHIC EXAMPLE, HAWAII TOOK GREAT PAINS IN A RENEWAL TO ASSESS FRANCHISE REQUIREMENTS THAT WOULD NOT PUT UPWARD PRESSURE ON RATES; THE CABLE SYSTEM RAISED RATES ANYWAY, PUSHING ITS PROFITABILITY WELL BEYOND ITS STATED GOALS.

In December, 1988, the State of Hawaii issued a franchise renewal order for Oceanic Cablevision. This order provided for a 15 year franchise in exchange for upgrades in two stages, the first to achieve 42 channel capacity by 1991. Significant requirements were also entered for public, educational and governmental access, island-wide institutional networking, and improved customer service. In assessing these requirements, the State attempted to phase in these costs so that the operator could meet its stated financial goals without having to raise rates. See summary of Oceanic franchise order at Exhibit C.

The State's desire not to be party to unjustified rate increases was so great that it retained professional consultants to determine just how far it could go in each year of the renewed franchise. Price Waterhouse completed a spread sheet analysis which pin-pointed exactly what costs could be imposed on Oceanic by the State without putting upward pressure on rates. Using financial assumptions and projections contained in Oceanic's own franchise renewal application, Price Waterhouse produced the study shown at Exhibit D.

Despite these efforts, Oceanic raised rates twice immediately following renewal of its franchise. The first increase of $1.65 a month in January was announced by Oceanic prior to the conclusion of negotiations and presumed in the Price Waterhouse study. A second increase of $1.70 came in March and this pushed Oceanic's financial performance well beyond the goals it set for itself in its renewal application.

What is sometimes exasperating for regulators is the ready manner in which the large MSO's seem to change their stated financial goals. ATC when it first purchased Oceanic in 1983 set a goal of 12% for profit and stated it would keep rate increases at approximately 1% per year.

When the application for franchise renewal was submitted in 1988, these goals remained the same. But once renewal negotiations had begun, Oceanic announced a much higher goal couched in different terms: a "cash flow margin" of 44%. A few months later, once the franchise was renewed, Oceanic again revised its goal upwards. Attempting to explain its second large rate increase in three months, Oceanic stated its cash flow margin goal would now be a phenomenal 50%, reflecting the new wishes of its parent, ATC (Time Inc.).

This willingness to cast aside promises and make new rules at a moment's notice does not do justice to the consumers of this nation. For MSO officers in New York, these decisions may merely reflect passing realities. For local system managers and state regulatory officials, these decisions can leave a long and bitter after taste. The unfortunate thing is that in the absence of true competition or rate regulation, these abuses will continue unabated.

VI. IF CONGRESS DOES NOTHING ELSE WITH THE 1984 CABLE ACT, IT MUST ACT TO ERADICATE "TRAFFICKING" IN CABLE SYSTEMS.

If the absence of competition is the principal cause of problems in cable regulation, then the worst single symptom of this problem has to be the churning of systems. When rates can be raised at will and consumers have no recourse, then it becomes easy to buy and sell cable systems several times over in a short period of time. Money needed to pay off succeeding piles of debt is presumed to be forthcoming from future rate increases. The problem is that no one is deciding when it will be too far--when the little system in Kapaa can no longer generate enough revenues to cover the mounting debt. And on the way to this point of collapse, no one is watching out for the consumer who is forced to pay exorbitant prices because he or she is in many cases unable to receive television without cable.

To the regulator, the high debt associated with trafficking can erode the ability of a system to honor its obligations to the community. These obligations may be as small as the addition of one more technicians to service disruptions, or as great as the promise to install full two-way wide-band voice, video and data capability between topographically separated communities.

As a practical matter, publicly traded MSO's will be open targets to hostile take-overs (a form of uninvited churning) so long as raiders believe they can cover their acquisition costs with future cable rate increases. If a repeat of the Time/Paramount scare is to be avoided, then rates must be re-regulated, and the sooner the better. As a matter of state policy, Hawaii has taken a strong stand in opposition to hostile take-overs of cable systems and the high debt associated with them. (See Hostile Takeover Policy at Exhibit E.)

In Hawaii, there are dangerous mountains of debt piling up in several of its cable systems. In this regard, Hawaii fully participates in the national trend. To cite a few examples:

1. Hawaiian Cablevision, recently acquired by United Artists/TCI and before that by Daniels, is generating $2.0 million in revenues a year. With this, it must cover $1.6 million in interest payments. This leaves too little to pay for operating expenses, improvements to the system and other community requirements. To cover the normal cost of operating the system, Hawaiian must borrow from a fund established by its parent. This is living on borrowed time, both literally and figuratively. It is no surprise that overnight Hawaiian doubled the rates it charges in the hotels and condominium associations which comprise the overwhelming majority of its subscriber base.[1/]
2. Sun Cablevision, also recently acquired by United Artists/TCI and Danieis, has a debt interest servicing requirement identical to Hawaiian Cablevision. It too must borrow from its parent to cover normal operating expenses.

[1/] This overnight doubling of rates applies to condominium associations but not to hotels.

3. Kauai Cable, the only system not yet owned by an MSO, is in the process of applying for transfer of the franchise to Intermedia. Preliminary indications are that the transfer price per subscriber will be $2500 to $3000. To pay this price, it appears that Intermedia will be forming a group of investors who will each in turn raise equity by borrowing. In effect, Hawaii will have yet another debt-ridden system foisted upon its ratepayers.
4. The biggest and most dangerous mountain of debt may potentially be Oceanic's, whose 206,000 subscribers may have to pay down a substantial portion of the debt that Time Inc. and Warner Communications acquired in their merger earlier this year. In avoiding a hostile takeover by Paramount Communications, Time's defensive merger with Warner has so far generated $11 billion in debt and as yet unstated interest obligations on preferred stock.

The important point is that Hawaii's ratepayers shouldn't have to pay for the debt of someone else's folly. Today's high rates are padding already high profits. To now fill padded profit margins with new debt would be unconscionable twice over. It is clear that if Congress succeeds in reinstating rate regulation, it must also be sure to permit regulators to review and if appropriate disallow present and future debt in the ratemaking. If the bad acts which followed the 1984 Cable Act are not to be compounded, future ratemaking must be made on a basis such as "return on original investment" and include the power to impose rate rollbacks.

VII. NONE OF THE ARGUMENTS ADVANCED BY THE CABLE INDUSTRY TO PROLONG THEIR UNFETTERED RATE INCREASES AND TRAFFICKING HAVE BEEN PERSUASIVE.

1. "We are making up for many years of losses when we raise rates today."

It is exceedingly ironic that MSO's who today own the systems in Hawaii are bemoaning the hard times and risks experienced--not by the MSO's--but by their mom and pop predecessors. By the time MSO's made their purchases, these systems were well past the frontier days when managers had to do everything by their own hand and existence was truly hand-to-mouth. Thus, when the MSO's came to Hawaii, they inherited systems which had already turned the corner. It is disingenuous for MSO's today to take credit for the suffering of their predecessors.

2. "We have to raise rates again because our programming costs keep going up."

Programming prices are fixed by the same people who claim their programming costs are rising. MSO's in

Hawaii which own important cable programming include ATC and United Artists/TCI. To base cable price increases on the pricing actions of affiliated entities, and then to complain about it, is to add insult to injury.

3. "Hawaii's cable rates are no higher than rates nationally."

The biggest problem here is that Hawaii's largest cable system, Oceanic, is the tenth largest in the U.S. With great economies of scale, it would be more logical to expect Oceanic's rates to be lower than the national average. This is not to say that high national average rates are justified or should be condoned. Furthermore, each system should be viewed on its own since each has unique costs, problems and values. A rate can only be seen in its own setting and national averages miss the point.

4. "Where pay channels made up for low basic rates all those early years, now basic must make up for declining pay revenues."

In Hawaii, there was an adequate return on original investment through basic cable revenues. If overall revenues from pay channels are declining, then it is incumbent upon the operator to find new sources of revenue. This is not unlike the time when operators had to be dragged to the altar to begin to use pay channels for the first time. It is likewise not convincing to hear that basic profits must be run up in order to make up for declines in other areas of business.

5. "Regulators are foisting stiff access and upgrade requirements upon us and we have no choice but to pass these costs on."

This argument might hold water if profits weren't so high. Again, reference is made to the Price Waterhouse study at Exhibit D which found further rate increases were unnecessary for the operator to meet the full range of State requirements.

6. "If required to lower rates artificially, we will be forced to 'unbundle' our basic tier."

This gets dangerously close to red-lining. The offering of a stripped basic package at a reduced price to some subscribers, like the elderly, is inherently objectionable. If doubts are entertained in this area, the issue of whether to allow unbundling of tiers should be left to the states and localities. Knowledge about the peculiar characteristics of a particular community can be better accommodated locally than by wide-ranging federal law. In Hawaii, there is no question that with 99% cabling and great distance over water to the next point of land, basic cable services should be generally available to the widest possible portion of the population. Further, unbundling can easily be prevented without changing the law--by putting language in franchise orders which specify that certain broad program areas like "a national news channel" and "a national sports channel" must remain in the basic tier.

VIII. HAWAII HAS ALREADY TRIED TO OBTAIN ADMINISTRATIVE RELIEF FROM THE FCC.

The State of Hawaii made attempts, mandated by state law, to win relief from rate deregulation. Staff visited the FCC to seek relief and found it futile to spend more state dollars with that avenue. A brief was filed at the FCC's recent "effective competition" rule-making--again to no avail. In Hawaii, only the remote desert area of Ka'u on the southern tip of the Big Island with its 933 subscribers merits rate regulation under FCC guidelines, and if this is only one of a few areas in the country to be eligible then administrative relief seems futile indeed. Hawaii believes it has exhausted its available administrative remedies.

IX. ACCORDINGLY, HAWAII BELIEVES IT HAS NO CHOICE BUT TO PRESS FOR LEGISLATIVE RELIEF AMENDING THE 1984 CABLE ACT TO PROVIDE FOR RATE RE-REGULATION.

Hawaii proposes that rate-making powers for basic cable service be returned to state and local governments. These governments already have in place the wherewithal to administer (or delegate with guidelines) uniform rate-making. They have Public Utilities Commissions which currently perform rate-making for power, transportation and intra-state telephone service. This regulation can and should serve as a model, whether cable goes exactly the same route or not.

Hawaii's own experience could also serve as a model as our law has always provided for a balance between the interests and needs of the cable systems and those of the public. This balance was maintained and served us well for 16 years--it has stood the test of time and experience.

Consequently, Hawaii has no objection to the return of regulatory power being coupled with explicit federal standards that promote equity for the consumer and a fair return to the cable industry. One possible option would be a hybrid arrangement where rates are unregulated as long as return on original investment does not exceed a specified level. Where operators wish their return on original investment to exceed this level, they would have the burden of proving the need for this to the states or localities.

SUMMARY

In summary, Hawaii believes that this is a critical juncture for restoring balance to cable rates and regulation. We respectfully request that the 1984 Cable Act be amended to give rate-making powers for basic cable service to state and local governments. Please let consumer protection again become a meaningful concept in the cable television field.

SUPPLEMENTAL STATEMENT

Conventional wisdom has reached the inexorable conclusion that America's cable television industry is not an open market--and has not been since the 5 percent rate increase caps were lifted on January 1, 1987. The State of Hawaii in submitting this supplemental testimony wishes to underscore the importance of simple solutions in consonance with the America's "open market" economy and the 1984 Cable Act's larger purposes.

I. A MODEL FOR RATE REGULATION SHOULD BE SIMPLE AND AVOID THE CREATION OF WINDFALL PROFITS.

Where there is only one multi-channel video provider to the community, Hawaii believes there should be a form of basic service rate regulation. Federal guidelines can provide the kind of compromise needed for re-regulation to gain acceptance by all affected parties.

For example, Hawaii would accept the tying of a floor for basic rate increases to the Consumer Price Index (CPI), with one important condition. The base date for fixing the CPI should be the last moment before competitive market forces first failed to take place. This was December 31, 1986. (On the next day, the last 5 percent cap, provided by the 1984 Cable Act, ceased to be in effect.) This would mean that rates in effect on December 31, 1986 would constitute the starting point for calculation of rates today. Rates then in existence would be raised by the CPI for each year since 1986 to figure out what the basic rate today should be.

This proposed floor would also be the floor below which regulators could not roll back rates any lower. In effect, this floor provides the cable operator with some degree of protection from patchwork rate re-regulation--and from potential "retribution" for any animosity that arose after the 1984 Act went into effect. Note that in addition operators are not being asked to rebate basic service revenues reaped in excess of the CPI during 1987-1990.

This date of December 31, 1986 constitutes the only starting date for federal guidelines consistent with the "open market force theory" that formed the basis for the 1984 Act. That is, where there is competition, rates need not be regulated; where there is an absence of competition, rate regulation becomes intrinsically rational. By setting the clock for federal guidelines back to December 31, 1986, the integrity of the 1984 Cable Act is thus preserved. Hawaii considers this the most important element of rate re-regulation.

At the same time, setting the clock back to December 31, 1986 swiftly overcomes any lingering after-effects from the FCC's inability to promulgate useful standards for "effective competition" in the face of inadequate market forces to moderate rate imbalance in the past three years. More importantly, if the clock is not set back to December 31, 1986, Congress will not only sanction but create "windfall profits". In effect, cable MSOs who correctly guessed that rates may be re-regulated--and raised rates greatly on the hope that the new rates would be grandfathered--will be rewarded. Those MSOs which were responsible about rate-setting during the past three years would be punished for having otherwise been good citizens.

Along with the setting of federal guidelines back to the date of deregulation, there should be some flexibility for higher rates, at the discretion of the local regulator. Such special rate increases could be granted by the local regulator as a reward for operating efficiently or for improved economies of scale or for improved consumer service. Or, these special rate increases could be granted for technological innovation, additions to community networking or extreme financial hardship unrelated to trafficking-acquired debt. The important point is to see that federal guidelines (e.g. setting the floor for rate increases to the CPI) can establish a minimum for rate increases. Even higher rates might be awarded under circumstances such as those envisioned above. Importantly, this leaves open the door for renewed cooperation between industry and government.

Tying the floor for rate increases to the CPI on December 31, 1986 is a simple, easily understood approach. It is practical and easy to apply. It offers the greatest consonance with the original purposes of the 1984 Cable Act which sought uniformity in rates and the promise that rate moderation would come from open market forces. This approach also avoids the creation by Congress of windfall profits. It provides the greatest amount of order and balance to an imbalanced marketplace. It promotes enhanced service and technology. It provides for reward to efficient operators. And it invites a quick return to non-adversarial relationships between industry and regulator. This model, simple enough, would correct the problems that arose from FCC inaction and the unanticipated absence of competition in the marketplace. In short, this compromise offers the quickest correction while maintaining maximum integrity with the original purposes of the 1984 Cable Act.

II. THE DANFORTH BILL HAS MANY IMPORTANT FEATURES BUT MAY UNINTENTIONALLY INVITE MORE DEBT AND VIOLATE THE CABLE ACT'S ORIGINAL PURPOSES.

Hawaii supports many of the provisions contained in U.S. Senate Bill 1880. The State's point-by-point discussion of the major elements of this bill appears in Appendix "A". Hawaii does, however, take exception with two provisions.

First, the bill would give rate regulatory authority to State and local governments where there is an absence of competition. We believe this would re-open the door to the kind of patchwork regulation that the 1984 Cable Act was designed to eliminate. Moreover, it could unleash a strong backlash of community ill will against cable operators, which although in some cases triggered by the prior conduct of operators, does nothing to restore positive relations. It could, in fact, lead to conduct by governmental agencies which would lead us back to where this all began a few years ago. What is needed is a balance, not a shifting of almost absolute power from government to the companies and then back to the government. Hawaii prefers a more uniform scheme as discussed above.

Second, the Danforth bill provides for the break-up of MSOs having greater than 15 percent of the market share. Hawaii strongly opposes this provision. It does not address the true problem which is the high debt acquired by MSOs at transfers, under a belief that rates can always be raised to pay off the debt. In fact, a forced break-up of large cable interests would likely exacerbate rather than relieve the artificial and unwelcome upward pressure that debt exerts upon rates--to wit, by superimposing yet another layer of debt associated with the new buy-outs. Rather than compound the atrocities of already high debt which slipped in through a temporary window of non-regulation and non-competition--Congress should now leave to business judgment and market forces the decision of how to gradually reduce debt. If, on the other hand, Congress reimposes rate regulation and forces a break-up, then Congress is creating a situation where ironically States and municipalities will have to approve future rate increases in order to cover the new debt payments inherited from the forced sale of these systems. It would be far simpler to let those who created the oligopolies find new ways to responsibly pay down their own debt from their over-expansive ways. Hawaii believes the ills of horizontal integration can for the most part be alleviated by rate re-regulation.

III. THE STATE OF HAWAII DOES NOT BELIEVE THAT TELCO ENTRY REPRESENTS A PANACEA FOR CURRENT PROBLEMS AND COULD IN FACT MAKE MATTERS MUCH WORSE.

The reservations about telco entry are substantial and can be summarized as follows:

1. The telcos do not have a track record as a "competitive" force having been monopolies through most of their existence. The logical fear is that at some point the cable companies would simply be gobbled up by the telcos. In any event, rate competition does not seem foreseeable with telco entry.

2. The financial structures and relative size of the entities differ greatly, with the telcos having the vastly upper hand.

3. The already strained pole arrangements would become a major battleground and a major source of litigation.

4. The dissimilar regulatory schemes would make any parity impossible and pose major burdens for federal and State regulators.

5. Since presumably the disappearance of the "wall" would work both ways, the potential desire of cable companies to get into the telephone business could pose major concerns in terms of risk to and dilution of resources on the cable side.

Put another way, the entry of another shark into the cable waters, presumably to compete with the sharks already in these waters, is not a substitute for the development of control and management mechanisms. In fact, if entry of another shark is desirable for other reasons, the issue of control and management becomes even more critical.

Hawaii believes that rate regulation remains the key issue, and that is true whether telco entry is permitted or not. At this time, Hawaii believes that without rate regulation, telco entry is inappropriate. And even with rate regulation, telco entry raises concerns that would need to be addressed.

IV. OTHER "CITY PANEL" QUESTIONS.

A. The Assertation That Rate Increases Have Been Accompanied By An Increase In The Number Of Programs Offered.

Hawaii's experience is that there are most often program changes which occur with rate increases and that the companies almost always attribute the rate increases in part to those changes. What also seems true however is that the actual increased cost to the company is only a fraction of the rate increase and cannot be said to "drive" the rate increases. And the correlation between rates and programming is made even more tenuous in the face of substantial profit margins and increased revenues from sources such as advertising.

B. Lifeline Services.

Hawaii's present basic tiers contain sufficient programming which (if rate re-regulated without unbundling) should be affordable to the elderly. This was the case before the 1984 Cable Act went into effect.

The cable industry's offer to "unbundle" in order to provide a cheaper tier for the elderly has emotional appeal- but may simply be an attempt to obfuscate the real issue. The real issue is whether having now run up basic rates to a point where consumers will object to further increases, the industry should now be permitted to convert the most popular basic channels like ESPN and CNN into new pay channels. This also raises the thorny question of whether Congress should act, in the absence of executive branch activity, to curb the vertical integration in the cable industry. This may be beyond the scope of these hearings on the 1984 Cable Act. In general, Hawaii strongly opposes the unbundling of existing basic tiers--unless Congress also grants full rate-making authority to local regulators.

C. Other Changes To Renewal Provisions.

Hawaii supports the amendments to renewal provisions contained in Senate Bill 1880. In addition, Hawaii recommends that purchase or sale of cable systems by franchising authorities be at market value less goodwill, and that legal appeal of renewal decisions first be required to exhaust both local administrative remedies and proceedings in the local courts.

D. PEG Access Channels.

Hawaii in implementing the 1984 Cable Act has imposed significant access channel requirements on Oceanic Cablevision, the nation's tenth largest cable system. The State intends to continue the course of implementing the access provisions of federal law, especially since significant community interest in PEG access has by now surfaced in most of the areas served by remaining systems undergoing franchise renewal.

E. Controversial Or Offensive PEG Programming.

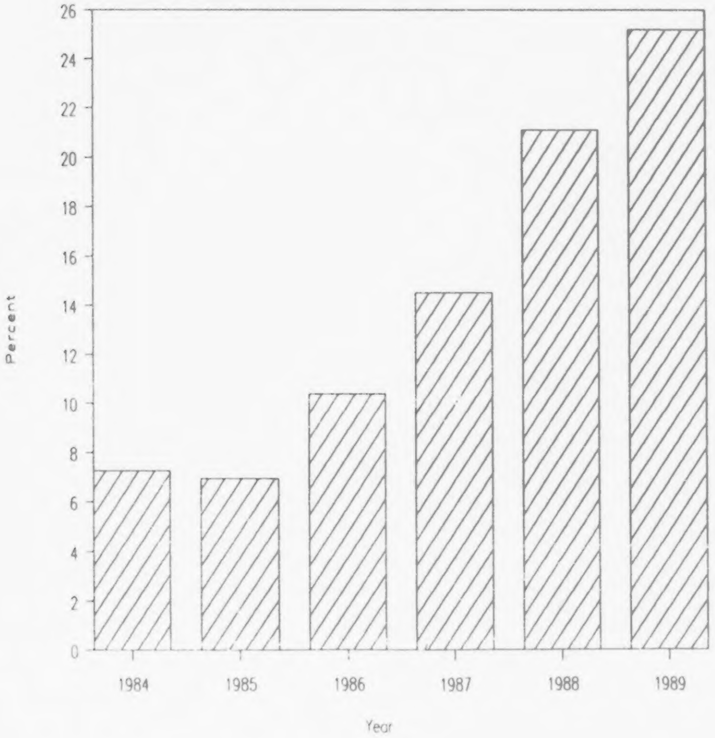
Hawaii has experienced strong public outcry on several occasions pertaining to obscene programming on the access channels. The State would welcome enhanced federally-authorized protections in this area, including the authority to limit such offensive programming without fear of civil liability.

Oceanic Cablevision

Year	Revenues (a)	Expenses (b)	Deprec'n & Amort'n (c)	Income from Operations (d)	Interest (e)	Net Income (f)	% Return on Revenues (g)
1984	$35,613,601	$27,005,923	$6,347,799	$8,607,678	$5,154,981	$2,587,697	7.27
1985	$48,509,822	$36,621,016	$8,275,184	$11,888,806	$6,346,994	$3,380,312	6.97
1986	$54,407,317	$39,375,084	$9,951,930	$15,032,233	$5,345,931	$5,654,832	10.39
1987	$61,939,494	$41,669,359	$9,814,476	$20,270,135	$3,631,690	$8,985,515	14.51
1988	$68,949,476	$45,603,722	$9,895,816	$23,345,754	$645,319	$14,539,854	21.09
1989 *	$55,640,426	$33,135,306	$8,972,246	$22,505,120	($1,130,107)	$14,015,371	25.19

* 9 Month totals including estimated income tax

Return on Revenues



Appendix "A"

State of Hawaii Comments on Cable Television Consumer Protection Act of 1989

(Senate Bill 1880)

Regulation of Cable Rates

New standard for effective competition. The State supports this new standard for effective competition. It provides a simple definition and description which removes confusion and controversy as to the plain meaning and intent of the standard under which regulation would be permitted. It allows an objective measure on which the question of regulation may be based.

Provision obligating franchising authority to consult with FCC and cable operators in establishing a fair and efficient method for regulating rates. Hawaii opposes this provision as it invites a return to the hodgepodge rate regulation the 1984 Act was designed to eliminate. Hawaii proposes a more simple and uniform system which limits rate increases where there is an absence of competition--as long as such limits are set back to the date of lifting of limits under the 1984 Cable Act (December 31, 1986). Hawaii supports uniform limits only if national sports programming remains in the basic tier.

Carriage of Local Broadcast Signals

Compulsory licensing and mandatory carriage of broadcast signals. Given the problems that the State has experienced in the past whereby Oceanic Cablevision preferred to carry its advertising and other programming in preference to UHF broadcasters who directed their programming to ethnic (Japanese and Korean) and religious broadcasting, the State strongly supports this provision. The UHF stations have been providing specialized programming which meets the needs of specific segments of our community which would not otherwise be met by other broadcast or cable sources. Sensitivity to these segments of our community would require that provision be made requiring cable systems to carry programming which they otherwise may not.

Franchise Renewal; New Franchise Issuance

New Proposals Allowed During Renewal Proceedings. Recent experience of the State with some renewal applications indicate that cable systems seek to provide the least amount of improvement in their facilities and services in exchange for the maximum cable franchise renewal term. This demonstrates a lack of incentive to propose the development of expanded cable facilities and services. The consideration of a competing new application at the same time as the renewal application will prompt the incumbent to submit innovative and creative proposals which in an efficient and effective manner will propose to improve the quality and quantity of cable services provided to the cable consumer. For these reasons the State supports this concept of application competition.

Flexibility In Considering Other Factors In The Evaluation Of Franchise Proposals. Given the unique composition and nature of the various communities in Hawaii, the State strongly supports this provision which allows franchising authorities to consider peculiar factors which are important to their franchise area. As our geography and sub-group needs are different from many other areas of the nation, this flexibility would enable us to have cable systems tailored to our unique community needs. To avoid undue vagueness, the process should provide for identification and publication of any special needs during ascertainment.

Changes In Denial Relief And Burden Of Proof. The State or local regulator must be presumed to have the best interest of its citizens in mind when evaluating applications for a permit or renewal, and should not in the absence of arbitrariness and capriciousness be subject to a de novo court trial of its decision. Since the cable operator is the one that is demonstrating its past fitness in providing cable services to the community, it should carry the burden of proof in showing why the franchise should be renewed. Consequently, the State supports this proposed change.

Time Windows For Consideration Of Renewal Application. The State in light of its experiences of the past two years supports more flexible time provisions for considering franchise renewal applications. The concern should be on carefully identifying quality cable communications services for the community rather than forcing all parties to comply with arbitrary timetables.

Regulation Of Services, Facilities, And Equipment

FCC to promulgate standards with franchising authorities allowed to make adjustments in the enforcement of these standards. The State recommends a change in this provision. The change would require the FCC to establish minimum standards for quality cable transmissions while allowing a State regulatory body to establish higher standards within reason and upon demonstration of the special needs of a given cable community.

Non-Discrimination With Respect To Video Programming

Prohibits anti-competitive practices in programming services. The State strongly supports this provision to insure that alternative multi-channel programming distributors have the services that will enable them to compete in the multi-channel distributor marketplace.

Acquisition Limitations

Establishes limitation of fifteen percent of cable subscribers as maximum for single ownership interest. Hawaii opposes this provision for the reasons stated in the text of this supplemental testimony to which this Exhibit is appended.

Senator INOUYE. Thank you very much. May I now call on the Councilwoman from the City of Bayonne, Ms. Dorothy Harrington.

STATEMENT OF DOROTHY E. HARRINGTON, COUNCILWOMAN, CITY OF BAYONNE, NJ

Ms. HARRINGTON. Good afternoon, Mr. Chairman and Mr. Gore. Thank you for affording me the opportunity to be with you this afternoon. I am an elected member of the Council of the City of Bayonne, and I am representing Mayor Collins. I also serve as Chairperson of Bayonne's Cable Television Advisory Committee.

The City of Bayonne occupies the three-mile-long peninsula dividing the waters of New York and Newark Bay. We have a population of slightly under 65,000 people, and we have a population that generally tends to stay in town. Consequently, we also have a very large senior citizen population.

In 1979, the city granted a ten-year franchise to Cablevision Systems Corporation. That franchise expired October 24 of this year. We began the renewal process with a series of negotiating sessions with Cablevision representatives, followed by public hearings held by both the advisory committee and the city council.

After two years of negotiation with the cable operator, we were unable to obtain a significant commitment from it to improve the quality of its service and to comply with several material terms of the initial franchise.

While Cablevision was seeking a ten to 15-year renewal of its franchise, it was not willing to commit to providing Bayonne subscribers with anything in the way of a high definition television signal when it becomes commercially available. I believe, Mr. Chairman, that high definition television is likely to be available within the next, say, five years.

In June, based on the city's review of Cablevision's past performance, its assessment of the community's future cable-related needs and interests, and Bayonne's citizens 'overwhelming expression of dissatisfaction with Cablevision, the City Council voted unanimously to deny the company renewal of municipal consent to operate a cable system in Bayonne.

I will not go into the details of the 16 findings. I have attached them to the reports that we sent forward. These findings are stated in the Council's resolution. Cablevision has petitioned the State Board of Public Utilities for a certificate of authority, notwithstanding the city's denial of its consent. And the parties are preparing for an administrative hearing.

The price for basic service in Bayonne is currently $17.95 a month. Compared to the lowest-price basic service available in 1979, that is a 298 percent increase. However, the number of channels offered with basic service has increased, and what was once cable operator's expanded basic is now our basic. You cannot buy that cheap rate any more.

So if you want to look at just that part, during the period of rate deregulation, from December 29, 1986, to today, the price of this expanded basic, which turned basic, has gone from $13.25 to $17.95 a month, an increase of over 35 percent. If we do not have the highest, we certainly have one of the highest basic rates in the country.

Bayonne was also one of the communities that suffered through the sports blackout which resulted from a recent contract dispute between Madison Square Garden, network and cable operators in the area. As a result of Cablevision's failure to come to terms on renewal of its contract with MSG, Bayonne subscribers were deprived of the ability to watch the Knicks, Rangers hockey and Yankee baseball games for over nine months.

During that time, Cablevision was able to increase the profits it made from its subscribers. Cablevision benefitted monetarily by avoiding payments to MSG while charging subscribers the same rate as when the service was being provided. The company brazenly continued to bill subscribers for service they were no longer receiving.

If any doubt remains as to whether the best interests of the consumer were being served by the MSG dispute, let me add one more fact. So that subscribers would not be deprived of the ability to see their home teams, MSG offered to allow Cablevision to continue carrying MSG programming for up to two years on the same terms as they had previously had in their contract. The proposal was rejected by Cablevision.

So you see, Mr. Chairman, it is Bayonne's experience that as a practical matter several of the stated purposes of the Cable Communications Policy Act of 1984 have not been accomplished. Congress believed that it would foster competition and technological innovation. Congress wanted to ensure that cable systems were responsive to the needs and interests of local communities.

But in the past five years we have not seen any significant improvements in the quality of cable services on most cable systems. We have not seen cable systems voluntarily providing any significant amount of programming geared to individual communities in which they operate. Cable companies seem to dictate the programs and services they will provide. We have not seen cable operators willing to invest their healthy profits either in new technologies.

What we have seen is the development of largely unregulated monopolies using their position as a monopoly to unfairly charge customers. What we have experienced in Bayonne is tremendous frustration on the part of local officials over the lack of accountability of cable operators and the city's loss of leverage in the franchise renewal process.

Cities are only now beginning to grapple with the meaning of the renewal provisions in section 626 of this Act. They will find, as Bayonne has, that the complex and ambiguous renewal provisions make it extremely difficult for the franchising authority to deny a franchise or a renewal of a franchise.

The renewal restrictions do not allow them to consider the quality or level of cable services that have been provided. Thus, cable operators have no incentive to provide quality cable service during their franchise term.

Combine this with rate deregulation, and the result is that cable operators may charge as much as they want for providing as little service as they wish. They still are entitled to renewal under Federal law.

Adding to the problem, cable companies have not shown an interest in competing with one another by building second systems in areas already served. So the renewal provisions of section 626 virtually guarantee a perpetual franchise to an unregulated monopoly.

To achieve the goals of the Cable Communications Policy Act of 1984, I would urge Congress to pass corrective legislative measures that would promote competition within the cable industry and encourage development other sources of multi-channel video programming as viable competitors to cable operators. Cities must be allowed to regulate rates charged by cable operators if consumers do not have a real choice in obtaining multi-channel video programming.

The FCC has ruled that effective competition exists if there are three over-the-air television signals that are present in a particular community. The FCC must be overruled in this regard with legislation that includes a realistic definition of "effective competition". I support Senate bill 833, which would redefine "effective competition" by looking at the number of multi-channel video programming distributors in a community rather than the number of over-the-air signals.

I also would ask Congress to act to prevent the kind of sports blackout that recently occurred in New Jersey, New York and Connecticut for a nine-month period. In its request for proposals for a franchise or franchise renewal, a franchising authority should be permitted to require that the cable operator carry all of the commercially-available video transmissions of the games of local professional sports teams, even if we pay for them.

Third, the Cable Act of 1984 should be amended to enable cities to deny franchise renewal where a cable operator has not provided adequate service. Under section 626, cities have been stripped of most of their bargaining power. The renewal process should be revised to permit franchising authorities to issue requests for proposals at the end of each franchise term.

By making the renewal process a competitive process, Congress would restore public accountability to the cable television industry.

I would also ask Congress to enhance competition in the cable television industry by permitting telephone companies to offer services competitive with cable operators. The presence of telephone companies as competitors should provide the necessary stimulus for greater diversity of services, better use of existing technologies and faster implementation of new technologies.

Very soon, cable franchises will be coming up for renewal in cities all over this country. Throughout the country, cable operators will be seeking to renew their franchises for long terms, long enough to extend into the next century. Will these cable operators submit proposals promising to provide the new services and technologies that our cities will need in the next century? Will cable operators bring us what they promised was the future power of cable when the initial franchise was granted?

At this moment, I think it is doubtful, given cable operators' track records to date, the limited regulatory authority of cities over cable franchises, and the general lack of competition in the cable television industry.

Thank you for letting me speak today.

[The statement and questions and answers follow:]

TESTIMONY OF
THE HONORABLE DOROTHY E. HARRINGTON
MEMBER, BAYONNE CITY COUNCIL
BAYONNE, NEW JERSEY

Good morning, Mr. Chairman and distinguished members of the Subcommittee. On behalf of the Mayor of Bayonne, Dennis P. Collins, and myself, I would like to thank you for affording me this opportunity to appear before you today. My name is Dorothy E. Harrington. I am an elected member of the City Council of the City of Bayonne, New Jersey. I also serve as chairperson of Bayonne's Cable Television Franchise Renewal Advisory Committee.

The City of Bayonne, located in Hudson County, New Jersey, occupies a three-mile long peninsula dividing the waters of the New York and Newark Bays. Bayonne has a population of slightly under 65,000 and has approximately 25,000 individual households. Bayonne is a town where families tend to remain in the same well-kept neighborhoods for many generations. Its residents are largely what you would consider blue-collar workers and come from diverse ethnic backgrounds. Over the last 15 years, the City has acquired a large senior citizen population.

In 1979, the City granted its consent to Cablevison Systems Corporation to construct and operate a cable television system in Bayonne. The New Jersey Board of Public Utilities subsequently issued the necessary certificate of approval for a ten-year franchise. That franchise expired on October 24th of this year.

We began the renewal process with a series of negotiating sessions with Cablevision representatives, followed by public hearings held by both the cable TV advisory committee and the City Council. After two years of meetings with the cable operator in an attempt to obtain a significant commitment from it to improve the quality of its service and comply with several material terms of the initial franchise, the City was unable to obtain anything more than a few general promises, so vaguely written as to be practically unenforceable. Cablevision was seeking a 10 to 15 year renewal of its franchise, and yet it was unwilling to commit to providing Bayonne subscribers with a High Definition Television (HDTV) signal or other HDTV services when such services become commercially available. As you know, Mr. Chairman, High Definition Television is in all likelihood going to be available to consumers within the next few years.

On June 14, 1989, based on the City's review of Cablevision's past performance, its assessment of the community's future cable-related needs and interests, and Bayonne citizens' overwhelming expression of dissatisfaction with Cablevision, the City Council voted unanimously to deny the company renewal of municipal consent to operate a cable system in Bayonne and recommended that the State Board of Public Utilities (BPU) deny the company a certificate of approval. I will not go into the details of the 16 specific findings on which the City Council based its conclusions that Cablevision breached materials terms of its franchise, that the quality of its service had not reasonably met the community's needs, and that its proposal for renewal did not meet the community's future cable-related needs. These findings are stated in the Council's resolution, a copy of which is attached as an exhibit to my prepared statement.

Cablevision has appealed by petitioning the BPU for a certificate of authority notwithstanding the City's denial of its consent. The case has recently been assigned to the State Office of Administrative Law for an administrative hearing.

The price for basic service in Bayonne is currently $17.95 per month. Compared to the lowest priced basic service available in 1979, that is a 298 percent increase. However, the number of channels offered with basic service has increased, and what was once the cable operator's "expanded basic" service is now the only basic service offered to new subscribers. Nevertheless, during the period of rate deregulation, from December 29, 1986 to today, the price of this "expanded basic" turned "basic" service has gone from $13.25 to $17.95 per month, an increase of over 35 percent. In addition, as of November 1, 1989, an additional increase of $2.00 per month has been put into effect for most of the service tiers other than the basic service tier.

If we do not have the highest, we certainly have one of the highest basic service rates in the country. And that is just basic service. Over 80 percent of Bayonne subscribers do not purchase basic service alone. After taking into consideration Cablevision's rates for additional sets, remote control units, and premium services, and the way in which the company bundles its premium services, thus requiring subscribers to pay for certain services they do not want in order to be able to purchase those that they do want, it is probably fair to say that the average monthly rate paid by Bayonne subscribers is higher than the average monthly rate paid by most households around the country.

The plight of the cable TV subscribers in the New York-New Jersey-Connecticut area received national attention when a sports blackout resulted from a recent contract dispute between the Madison Square Garden Network (MSG) and cable operators in the area. Bayonne was one of the communities affected by that dispute. And because Cablevision was the last cable operator to come to an agreement with MSG, Cablevision subscribers, in particular, were the ones most affected by the dispute. As a result of Cablevision's failure to come to terms on renewal of its contract with MSG, Bayonne subscribers were deprived of the ability to watch New York Knicks basketball games, New York Rangers hockey games, and New York Yankees baseball games from September 14, 1988 through July 5, 1989. Bayonne residents, along with thousands of subscribers in the tri-state area missed the entire 1988-89 Knicks and Rangers season, and half of the Yankees season.

The paradox in this situation was that during the time that Cablevision and MSG were without a contractual agreement, Cablevision was able to increase the profits it made from its subscribers. Cablevision had been paying MSG a certain price per subscriber, on a total subscriber basis. When Cablevision discontinued its carriage of MSG, it benefitted monetarily by avoiding payments to MSG while still charging subscribers the same rate as when the service was being provided. The company brazenly continued to bill subscribers for a service they were no longer receiving.

If there is any doubt remaining as to whether the best interests of the consumer were being served during the contract dispute with MSG, let me present one more fact. So that subscribers would not be deprived of the ability to see their home teams while the dispute continued, MSG offered to allow Cablevision to continue carrying MSG programming for up to two years on the same terms as the expired contract. This "standstill" proposal was rejected by Cablevision.

As you can see Mr. Chairman, it is Bayonne's experience that, as a practical matter, several of the stated purposes of the Cable Communications Policy Act of 1984 have not been accomplished as a result of the statute's implementation. When the Act was passed, Congress believed that it would foster competition and technological innovation. Congress wanted to ensure that cable systems were responsive to the needs and interests of the local community. But in the past five years we have not seen any significant improvements in the quality of cable services on most cable systems. We have not seen cable systems voluntarily providing any significant amount of programming geared to the individual communities in which they operate. We have not seen cable operators willing to invest their healthy profits in new technologies.

What we have seen is the development of largely unregulated monopolies in the delivery of cable TV services, using their position as a monopoly to unfairly charge consumers for those services. What we have experienced in Bayonne is tremendous frustration on the part of local officials over the lack of accountability of cable operators and the City's loss of leverage in the franchise renewal process.

Cities are only now beginning to grapple with the meaning of the renewal provisions in Section 626 of the Act. Unfortunately, they will find, as we in Bayonne have, that the complex and ambiguous renewal provisions make it extremely difficult for a franchising authority to deny a cable operator renewal of its franchise. The renewal restrictions imposed upon franchising authorities do not allow them to consider the quality or level of cable services that have been provided. Thus, cable operators have no incentive to provide quality cable service during the franchise term.

Combine this with the 1984 Act's elimination of rate regulation and the result is that cable operators may charge as much as they want for providing as little service as they wish, and still they are entitled to renewal under federal law. Adding to the problem, cable companies have not shown an interest in competing with one another by building second systems in areas already served, otherwise known as "overbuilds." So the renewal provisions of Section 626 virtually guarantee a perpetual franchise to cable operators that hold unregulated monopolies.

To achieve the goals of the Cable Communications Policy Act of 1984, I urge Congress to pass corrective legislative measures that will promote competition within the cable industry and encourage development of other sources of multichannel video programming as viable competitors to cable operators.

First, Cities must be allowed to regulate rates charged by cable operators if consumers do not have a real choice in obtaining multichannel video programming. The FCC has ruled that effective competition exists if three over-the-air television signals are present in a particular community. This standard precludes over 90 percent of the franchising authorities in the country from regulating cable rates. The FCC must be overruled in this regard with legislation that includes a realistic definition of "effective competition." I support Senate Bill 833 which would redefine "effective competition" by looking at the number of multichannel video programming distributors in a community rather than the number of over-the-air signals. Senate Bill 833 would reasonably define effective competition as a situation where at least 67 percent of households in the community have service available from a competing unaffiliated distributor, and more than 30 percent of the community's cable subscribers subscribe to the competing distributor.

Second, Congress should act to prevent the kind of sports blackout that recently occurred in New Jersey, New York and Connecticut for a nine-month period. In its request for proposals for a franchise or franchise renewal, a franchising authority should be permitted to require that the cable operator carry all of the commercially available video transmissions of the games of local professional sports teams. There is currently pending in the House of Representatives Bill 2363, which includes language that would give communities this protection.

Third, the Cable Act of 1984 should be amended to remove the impediments to the ability of cities to deny franchise renewal where a cable operator has not provided adequate service. Under Section 626, cities have been stripped of most of their bargaining power. The renewal process should be revised to permit franchising authorities to issue requests for proposals at the end of each franchise term.

By making the renewal process a competitive process, Congress would restore public accountability to the cable television industry. If the cable operator has not been offering a quality product at a fair price, the marketplace will demonstrate as much.

Instead of receiving a franchise in perpetuity, the cable operator will receive an appropriate return on his investment, as the Act already provides.

Fourth, Congress should enhance competition in the cable television industry by permitting telephone companies to offer services competitive with the cable operators. The presence of telephone companies as competitors in the industry should provide the necessary stimulus for greater diversity of services, better use of existing technologies, and faster implementation of new technologies. Of course, we do not want to see cable company monopolies replaced with telephone company monopolies, and therefore, in return for being permitted entry into the video services market, they must agree to local regulation and local franchising provisions.

Very soon, cable franchises will be coming up for renewal in cities all over this country. Throughout the country cable operators will be seeking to renew their franchises for terms long enough to extend into the next century. Will these cable operators submit proposals promising to provide the new services and technologies that our cities will need in the next century?

Will cable operators commit themselves to bringing us what they promised was the future power of cable when the initial franchise was granted: the power to broaden educational opportunities; to increase employment opportunities for those who can only work at home; to improve our competitive position through direct access to data networks; to allow monitoring of water systems and synchronization of traffic signals; to permit in-home shopping and banking? At this moment that is very doubtful, given cable operators' track record to date, the limited regulatory authority of cities over cable franchises, the cities' inability to seek competitive bids at franchise renewal, and the general lack of competition in the cable television industry.

OVERSIGHT OF THE 1984 CABLE ACT

ANSWERS TO POST-HEARING QUESTIONS FOR COUNCILWOMAN DOROTHY E. HARRINGTON

QUESTION NO. 1

> In response to concerns over rate increases, the cable industry has pointed out that the rate increases have been accompanied by an increase in the number of program services and that the cost to the subscriber for each program service has only increased by an average of one penny. What is your response to these contentions?

ANSWER

The City of Bayonne does not believe the industry's analysis of the average cost increase per program service to be an accurate reflection of what has occurred in Bayonne. During its original franchise term, in addition to providing new program services, several program services have also been dropped by the cable operator. The price of basic service in Bayonne has increased from $13.25 to $17.95 per month, a 35 percent increase, during the period of rate regulation. In that same period, considering both the added and deleted programming services, the net change is an addition of only one or two channels during the period of rate deregulation.

Moreover, since cable operators are unwilling to upgrade or rebuild systems to increase channel capacity during the term of the franchise, at this point additional programming services can only be provided by cable operators if other services are deleted or if channels are shared with other programming services. Even in the case of a shared channel, consumers must to some extent sacrifice one programming service in order to gain another.

If the cable industry wishes to focus on the increase in the number of program services available since cable's inception, in fairness, that increase must be compared with the lowest priced basic service tier that was also available at cable's inception in Bayonne. This lower-tier basic service is no longer available in Bayonne, except to those who originally subscribed to it. Thus, while additional services may now be available, the lower-tier basic service is no longer available in Bayonne (with the above-noted exception) and the cost of "basic" service with the so-called additional program services has risen from $4.50 to $17.95 per month, an increase of 298 percent. This is hardly an increased cost of one penny per program service!

In the near future, any benefits to subscribers from an increase in programming services will be nullified as cable operators begin shifting services from "basic" to "pay" channels, as is likely to be done soon with ESPN. The City is not optimistic that the loss of ESPN from basic service would be accompanied by an appropriate reduction in the price of basic service.

Furthermore, Cablevision is currently experimenting in New York City, with what it calls "segmented basic service," where the programming services presently included in basic service must be purchased a la carte, in "clusters." The result will be that the total cost to purchase all of the clusters will exceed the current cost of purchasing all of the same programming as basic service.

QUESTION NO. 2:

> If we were to flat fee for a basic cable or "lifeline" service, what program services should be

included in that basis tier and what should the price be?

ANSWER

A lifeline service should include all broadcast stations that are significantly viewed in the franchise area, all public, government and educational access channels, and any other channel on which the cable operator provides local origin programming.

"Significantly viewed" should be defined to include, at a minimum, those broadcast stations that were required to be carried under the FCC "must carry" rules. In light of the fact that such "lifeline" service includes far fewer program services than are provided in what most cable operators currently designate as their basic tier, the price for "lifeline" service should also be considerably lower. A monthly charge of $5.00 would be reasonable.

QUESTION NO. 3:

What other changes in the renewal provision do you feel are necessary?

ANSWER

The renewal provision of the 1984 Cable Act should be revised to permit franchising authorities to request competitive proposals at the end of each franchise term.

Section 626(c)(1)(B) should be amended to permit consideration of the reasonability of the mix, quality or level of cable services or other services provided over the system. Cable operators' interests would be adequately protected by language that requires the quality of the operator's service to be evaluated in terms of reasonability "in light of community needs." This revision would make the renewal criteria more consistent with sections 624(b)(2)(B) and 625(a)(1)(B) of the 1984 Act, which were intended to protect a franchising authority's ability to require broad categories of programming and to preserve the mix, quality and level of services required in a franchise agreement.

The 1984 Act should be amended to make clear that a franchising authority may not only require a certain mix, quality and level of services, but may require that such a mix, quality and level of services be preserved on the cable operator's basic tier, excepting any "lifeline" service established by Congress or the cable operator.

The 1984 Act should be amended to include language stating that any mutually agreed to requirement may be included in the franchise regardless of the provisions of the Act.

QUESTION NO. 4:

> You support elimination of the restriction on telephone ownership of cable systems. How will this enhance competition since under most estimates, the broadband network will not be in operation for decades?

ANSWER

The City of Bayonne is not in a position to evaluate the reasonableness of the premise upon which the question is based, *i.e.*, that "the broadband network will not be in operation for decades," and accordingly is unable to answer the question as framed. However, assuming the truth of this assertion, if it is in fact Congress' assessment that consumers would benefit from competition in the cable television market, then, in the City's view, it would not be an adequate ground for refusing to permit such competition that it may take several years to implement competing technology. In fact, the knowledge that competing technology is in the process of being developed will probably be the only effective incentive for current cable system operators to develop advanced technology of their own.

The fact that telephone ownership of cable systems might not enhance competition in the cable industry in the immediate future, would support the City's position that the renewal provision in the 1984 Act should be amended to make the renewal process a competitive process.

QUESTION NO. 5:

> Do your franchise agreements require the provision of public access channels?

ANSWER

Under the franchise agreement which expired in October 1989, Cablevision did not provide an exclusive public access channel, but did agree to air public access programming on its local origination programming channel, which is a shared channel that has also been providing "cherry-picked" programming from distant broadcast stations.

QUESTION NO. 6:

> Have your cities encountered any difficulties with controversial or offensive programming carried on your public access channels?

ANSWER

No.

Senator **Inouye**. I thank you very much, Ms. Harrington.

Mayor Ramirez.

STATEMENT OF SAUL N. RAMIREZ, MAYOR, PRO-TEM, CITY OF LAREDO, TX

Mr. **Ramirez**. Thank you very much, Mr. Chairman, Senator Gore. This will be a short summary statement. My written testimony has been submitted to the Committee.

My name is Saul N. Ramirez, Jr., and I am an elected member of the City Council of Laredo, Texas, and Mayor Pro-Tem of the City.

Thank you for the opportunity to appear here today for the City of Laredo.

In 1984, the Cable Act was part compromise and part theory about how competition to cable would develop. It is time for a reality check on the implementation of the theory.

The Cable Act of 1984 must be reformed. I believe this for several reasons.

First, the theory of the act has proven to be flawed. Second, in Laredo, competition simply is not. Third, cable is essential for adequate television. And fourth, cable consumers know they are being victimized.

Congress' theory in 1984 was superficially attractive: deregulate cable and competition would naturally control cable operator behavior.

Had we testified then, we would have warned you that the theory did not parallel reality. Cable, once built, is a monopoly. Broadcasting is not competition to cable. Cable is a transmission medium all programmers must use to reach the homes of cable subscribers.

In Laredo, effective competition is nonexistent. Laredo is isolated geographically, devastated economically, and overwhelmingly a Spanish language community.

Laredo is the second poorest MSA in the entire Nation.

In 1987, 37 percent of our families were below the poverty level. One in four of our citizens speaks no English, and about 94 percent of our people speak Spanish as their primary language of choice.

People in Laredo must rely on cable for television in their language and feel tied to cable as a fundamental necessity. Despite the extreme poverty, cable penetration is nearly 86 percent.

Penetration has increased to that level despite four increases since deregulation. Basic rates today are 258 percent of their 1984 level.

Basic now costs $17 per month. The rate in 1984 was $6.60.

Yet, during this time, cable penetration actually has increased. This shows market power, inelastic demand, and a lack of alternatives.

Why does the cable operator have unrestricted pricing power in Laredo when, under FCC theory, Laredo prices should be restrained by competitive forces if there are three television signals?

Well, first, we have only one over-the-air Spanish language signal, and it is a low power one.

Second, we are highly dependent on the services available, principally through cable. For us, cable is an essential window to the world. And, as with other utility services, we cannot disconnect, no matter what the price.

Cable is essential for adequate television.

Congress must recognize that cable is often essential and should be regulated like a public utility. Cable service is delivered for a fee under public franchise over public property. To allow it to be priced without restraint denies the reality of our people's lives.

Consumers know they are being victimized.

Today, cable operators have little incentive to offer high quality service that is fairly priced. A recent example in Laredo is the realignment and higher price for Spanish language signals.

On September 1, the operator moved two key Spanish signals and the practical consequence is that Spanish-speaking households without cable ready sets must pay an extra $5.50 per month to receive three Spanish channels.

We believe this violates our franchise, and the cable company cites the Cable Act as its authority to do so.

It would be costly for us to litigate. So the realignment and higher costs continue.

Senator, like you, I am an elected official. Like you, I serve our people with pride and want to protect them from unfair treatment.

We must work together to restore regulatory sanity and competitive balance to the cable marketplace. I believe in competition and fairness. For these to happen, Congress must empower us to restrain unfair pricing by cable monopolies.

When Ted Rogers sold our system, Laredo exported $55 million from the pockets of citizens and consumers into a Canadian bank. That was five times more than what he paid for the system just eight years earlier.

What do we have to show for it? The same limited capacity cable system, but with reduced service, fewer jobs, more expensive Spanish programming, and dramatically increased rates.

It is as if an unbridled horse were trampling consumers and the community.

Let us pull back the reins and restore the balance. To do this, we ask your help in reforming the Cable Act.

Thank you.

[The statement and questions and answers follow:]

STATEMENT OF SAUL RAMIREZ, MAYOR PRO-TEM
AND CITY COUNCILMAN, CITY OF LAREDO, TEXAS

Mr. Chairman and Members of the Subcommittee:

INTRODUCTION

My name is Saul N. Ramirez, Jr. I am an elected member of the City Council of the City of Laredo, Texas, and Mayor Pro-Tem of the City. I am pleased to have the opportunity to appear here today on behalf of the City of Laredo.

In 1984, Congress enacted the Cable Communications Policy Act. It was part compromise between the main parties, and part theory about how cable competition would work to benefit and protect the public at large. In this fifth year of implementation of the Cable Act, it is appropriate and necessary that Congress test whether those theories have matched reality. In other words, it is time to do a "reality check" to see whether and how the theories are holding up in practice and in implementation.

Like the other members of this panel, I believe the public record surrounding the implementation of the Cable Act of 1984 is clear and convincing: The Cable Act must now be reformed.

I. THE THEORY OF THE 1984 ACT IS FLAWED.

The theory Congress used in 1984 was superficially attractive: Deregulate the cable industry, and let competition control cable operator behavior.

But if you had asked us in Laredo to testify then, we would have warned you that the theory did not parallel the reality, at least in our experience and circumstances.

Cable, once built, is a monopoly.

Broadcasting is not competition to cable. Cable is the transmission medium all programmers, including broadcasters, must use to reach the television sets in the homes of cable subscribers.

But to most of the nation -- the 80% still unserved by cable in 1983 -- the theory made sense. So Congress acted.

Attached to my statement is a "White Paper" and an "Addendum" to that White Paper which discuss the historical accident of political forces that allowed the 1984 Cable Act to become law. I commend these documents to your attention.

In summary, the White Paper describes how cities, other local franchising authorities and consumer groups were the only significant organized political groups arguing for continued regulatory protection of consumers in the 1984 Congressional debate. The cities assumed that the final version of the Act did preserve substantial consumer protections. The cities, like the Congress, assumed that cable would continue to be rate regulated wherever it was not subject to "effective competition", and would continue to be subjected to franchising to ensure that it delivered its promised services in individual communities.

In reality, however, since 1984 neither assumption has proven correct. The remainder of my statement will illustrate what has happened to each assumption. First, I will describe the social experiment of rate deregulation and its impact on Laredoans -- residents of the second poorest Metropolitan Statistical Area in the United States. Then I will mention recent examples in Laredo of how our cable operator, under the current structure of the Cable Act, is taking advantage of the consuming public.

II. IN LAREDO, "EFFECTIVE COMPETITION" ISN'T.

The Federal Communications Commission (FCC), under then Chairman Mark Fowler, adopted "the presence of three broadcast signals" standard for measuring "effective competition" in a cable community. This effectively deregulated nearly 100% of the cable homes of the nation.

Consider the effect that ruling has had in Laredo. We are relatively isolated geographically, disadvantaged economically and, overwhelmingly, are a Spanish language cable community. In terms of geographic location, we are in extreme south Texas on the Mexican border, with Mexico a bridge away across the Rio Grande River. We are approximately 150 miles to the nearest

American city, San Antonio, and the area in between is relatively unpopulated.

Economically, of the 275 largest Metropolitan Statistical Areas listed by the U.S. Department of Commerce, Laredo has the second highest percentage of population living below the poverty level. In other words, Laredo is the second poorest Metropolitan Statistical Area in the entire nation. In 1980 30% of our families were below the poverty level. By 1987 the percentage had increased to 37%. In 1980 the median income in Laredo was only $10,603. In 1987 the unemployment rate was nearly 16%.

In addition to our geographic and economic isolation, one in four of Laredo's citizens speaks no English at all. These Laredoans rely exclusively upon Spanish. Three out of four of our citizens speak Spanish as the language of the home, and more than 9 out of 10 -- about 94% -- of our people speak Spanish as the primary language.

People in Laredo must rely upon cable television for television programming in their language, and have felt tied to cable as a matter of fundamental necessity. Despite the extreme poverty of the community, cable penetration is extraordinarily high -- nearly 86% -- and has remained at that level notwithstanding four successive increases in basic cable rates since the rate deregulation provision was enacted only five years ago. Basic rates today are 258% of their 1984 level ($17.00 per month in 1989, as compared to $6.60 per month in 1984). Yet, during this time, cable penetration actually has increased, suggesting a true inelasticity of demand and a lack of alternatives to cable.

Nor does the recent history of transfers of control of the Laredo cable system suggest that anything like "effective competition" is, has been, or will be occurring. Even the recent sales documents for the system suggest a monopoly with pricing power -- prices driven solely by demand, not by the give and take of competitive forces.

Only two years ago, in October 1987, Rogers Cable Systems of the Southwest planned to sell the Laredo system to the Adam Corporation for $46 million, or $1,875 per subscriber. (The Adam Corporation later elected not to complete the purchase, but did buy two other cable systems which it kept only a few months before "flipping" them at a profit of $12 million; Adam then went into the savings and loan business.) By August of 1988, Rogers arranged to sell all of its U.S. systems to KBLCOM for $1.3 billion, or about $2,600 per Laredo subscriber.

Both the seller of the cable system, Rogers Cable Systems of the Southwest, Inc., and the buyer, KBLCOM, Inc., a subsidiary of Houston Industries, Inc., promoted the sale based upon evidence that Laredo is not subject to effective competition forces which limit an operator's ability to increase prices. They expressed it this way:

> The Laredo System has many of the characteristics of a "classic" cable system. "Classic" cable systems are typified by a scarcity of over-the-air broadcast channels otherwise available to potential subscribers in the service area and a perception that cable is a necessity rather than a luxury. In addition, the

> Laredo system has maintained a stable subscriber base despite a relatively depressed economy, and three separate rate increases implemented over the past two years.

Rogers used this language in its prospectus for potential buyers, and KBLCOM used it in its solicitation of financing for the purchase.

Why does the cable operator have unrestricted pricing power in Laredo when the FCC's theory holds that Laredo prices should be restrained by competitive forces simply because there appear to be three Grade B over-the-air signals?

There are two main reasons. First, we have only limited over-the-air Spanish language television in Laredo. For our community, with its extraordinary utilization of Spanish, the availability of English language programming is not relevant to whether the competition to cable from over-the-air broadcast service is "effective" enough to warrant the complete deregulation of basic cable rates.

Second, our community is highly dependent on the cultural and intellectual and entertainment services available principally through the cable system. For us, cable is essential. As with other kinds of utility services, we cannot disconnect, no matter what the price. We think we have adequate justification for an FCC exception based on the particular combination of circumstances that prevails in Laredo. But we also believe Laredo is a symbol of a broader problem with the Congressional approach to cable rate regulation as implemented by the FCC.

III. CABLE IN LAREDO IS ESSENTIAL FOR ADEQUATE TELEVISION.

We believe cable television in a community like Laredo is not a luxury. It is time for Congress to recognize that across the country, cable is an essential service and should be regulated like a public utility. Adequate television service and programming are essential for working people in Laredo trying to improve their state in life, and for citizens to overcome the language barrier to full participation in the democratic process. The cultural, educational and entertainment role that television plays in a geographically isolated, lower income community like Laredo is critical. To suggest that this service, when delivered for a fee by cable under a public franchise and using public property, should be priced without restraint, denies the reality of our people's lives.

To the working poor, basic cable at $17.00/month is the only entertainment and cultural experience they can afford. Disconnecting as the price doubles or triples is not an alternative. That is why penetration is so high and demand so inelastic.

Mr. Chairman, adequate television, like adequate electricity, is essential to our quality of life. Disconnecting cable service is no more realistic to a family in Laredo than is disconnecting electricity. For us, at least, there is no other realistic alternative.

We believe that a re-examination by the Congress of the theory and implementation of the effective competition provision of the Cable Act is overdue. Laredo is an example of Congressional intent gone awry in this regard, and a case study of a wide gap between legislative theory and the reality of its implementation.

IV. CONSUMERS KNOW THEY ARE BEING VICTIMIZED.

Today, cable operators have little or no incentive under the present regulatory regime to provide consumers with high quality cable television service that is fairly priced. Two examples of this lack of incentive are now occurring in Laredo.

A. Removal of customer service representatives

A cable operator needs cash flow -- not satisfied customers. Generally, it appears from our observations that an operator will not spend an additional dollar if that expenditure does not yield additional cash flow. That is why so many cable systems provide terrible signal quality, fail to answer their telephones, ignore franchise service commitments, and are slow to correct billing errors and other consumer abuses. Once a home is hooked to the cable, the operator need only provide service good enough to avoid disconnection. Spending a dollar on repair personnel and telephone operators will not yield additional revenue from existing subscribers, who simply have nowhere else to go. So the cable owner says to the system manager: "Save the money, it won't generate additional cash flow."

This exact problem occurred in Laredo only last month. Our cable operator has always employed local customer service representatives, all of whom speak Spanish, to handle telephone inquiries. But, recent press reports and company statements indicate that the company has decided to increase its cash flow by relocating all its customer service representatives to a central location in San Antonio and by firing Laredo employees. Our local system manager stated in a public hearing to our Cable Commission in September that this "rumor" was false. A company representative has said that in early 1990 Laredo customer service representatives will be given notice of termination.

B. Realignment of Spanish language signals relied upon in the community.

On September 1, 1989, in conjunction with a general rate increase and without notice to Laredo subscribers, KBLCOM realigned several signals on the cable system in Laredo. We believe this action violated the terms of our franchise contract.

Two signals in particular have caused serious concern to the consuming public and to the City. Despite the nearly unique importance of Spanish language programming in the community, Univision (SIN) was moved from Channel 7 to Channel 32, and XHBR-TV (the Mexico City broadcast signal) was moved from Channel 11 to Channel 33. Both Univision and XHBR-TV remain available on basic, but only as part of an expanded, and significantly more costly, basic service, which for most viewers involves both a rate increase and the need to rent a converter.

The channel realignment, together with rate structure changes, produced a net increase of $5.50 per month for new subscribers after September 1, 1989. This occurred shortly after representations by the company that basic rates would remain unchanged.

The company cites the Cable Act as its authority for this action; it claims that the Act allows "retiering", but that concept is not defined. The City disagrees with the company's interpretation. We do not believe that Congress intended cable operators total freedom in realigning their cable channels. But our only recourse is to take the company to court and initiate major litigation seeking a precedent setting interpretation of the Cable Act.

If we were successful, the company would have to shift the services back, but we would have to pay our litigation expenses. It is unlikely we can recover damages or consumer refunds. Whether or not the company is successful, it has enriched itself substantially by grabbing valuable channels for its own programming. This more than compensates for its costs in defending the litigation. And every day that goes by the company is enjoying unfair profits from the service shift at the expense of the poorest residents of our City.

This incident therefore illustrates that the Cable Act in reality has distorted local efforts to protect consumers and rendered such efforts ineffective or prohibitively expensive for local franchise authorities.

CONCLUSION

Senators, like you, I am an elected official. Like you, I serve our people with pride and want to protect them from unfair treatment. We have to act together to restore regulatory sanity and competitive balance to the cable television marketplace.

I believe in competition. Our people ask only for the opportunity to participate in a fair marketplace. We will do the rest through hard work and education. But the Congress has to protect us from unfair pricing by this monopolistic industry. We in Laredo have exported fifty-five million dollars from the pockets of Laredo citizens into Ted Rogers' Canadian bank. That is five times more than he paid for the cable system just eight years earlier. What do we have to show for it? We have the same limited capacity cable system, reduced levels of service, fewer jobs, more expensive Spanish language programming, and dramatically increased subscription charges.

We ask your help in restoring the balance and fairness which were the goals of the Cable Act theory, but which have not been realized in reality.

Thank you.

SUPPLEMENT TO STATEMENT OF SAUL RAMIREZ, MAYOR PRO-TEM AND CITY COUNCILMAN, CITY OF LAREDO, TEXAS

January 17, 1990

Hearing on the Oversight of the
1984 Cable Telecommunications Act
United States Senate
Communications Subcommittee
November 16, 1989

1.) Question: In response to concerns over rate increases, the cable industry has pointed out that the rate increases have been accompanied by an increase in the number of program services and that the cost to the subscriber for each program service has only increased by an average of one penny. What is your response to these contentions?

Answer: With respect to Laredo, the contentions are misleading and miss the point. As indicated in Mayor Pro-Tem Ramirez' testimony (at page 4), Laredo has the second highest percentage of population living below the poverty level of the 275 largest Metropolitan Statistical Areas in the United States. In 1987, 37% of Laredo families lived below the poverty level, and unemployment was nearly 16%. In this context it is of little relevance that the 258% increase in rates for basic cable service since 1984 occurred during a period when additional programming was added.

There have been four rate increases, only the last of which was accompanied by a simultaneous increase in program channels. In that instance, which occurred this past Fall, basic service was expanded from 24 to 34 channels, the sum total of all non-pay activated channels on the entire cable system. As a result, no subscribers can choose less than the full 34-channel non-pay offering of the system, although the only non-pay option is still characterized as "basic"; the choice is all 34 channels or no cable service. In fact, the cost of the lowest level of service available jumped from $11.50 to $17.00 on October 1, and since then no subscriber has been able to choose any more affordable, "lifeline" level of program choices. The increase in program channels, then, rather than justifying the unwanted rate increases, has become merely part of the method of implementing them.

This change, implemented in September, 1989, was accompanied by an increase in the rate for basic service for new subscribers from $13.00 to $17.00 per month. Over and above this increase, the change also necessitated rental of converters -- at an extra monthly charge of $1.05 per television set -- to receive channels on the "expanded basic" but not needed by many subscribers previously. As a result, the channel realignment, together with rate structure changes, produced a net increase of $5.50 per month for new subscribers (plus converter rental) after September 1, 1989 (Ramirez testimony, page 10).

In 1984 the basic tier contained thirteen channels and cost $6.60 per month. In Laredo, the owners of the cable system themselves have characterized the system as "classic", meaning typified by "a scarcity of over-the-air broadcast channels ... a perception that cable is a necessity rather than a luxury ... the Laredo system has maintained a stable subscriber base despite a relatively depressed economy, and three separate rate increases implemented over the past two years." (Ramirez testimony, pp. 5-6).

Though channels have increased in Laredo, consumer choice has been eliminated, and the cost of receiving any cable service has gone up 258%. In enacting the rate regulation provisions of the Cable Act in 1984, Congress intended that rates for basic service could be regulated (so as to remain affordable) wherever there is no "effective competition". This intent has been defeated in Laredo, where rates have skyrocketed notwithstanding the lack of effective competition as effectively conceded by the system operators themselves. The fact that program services have been increased is not an answer to the policy concerns now being raised and needing to be addressed in legislation.

2.) Question: If we were to adopt a flat fee for a basic cable or "lifeline" service, what program services should be included in that basic tier and what should the price be?

Answer: To be "lifeline", service must be keyed to community needs, responsiveness to which is one of the stated goals of the Cable Act. What is "lifeline" in one community may not be in another. To be implemented effectively, therefore, the "lifeline" concept must include a role for the franchise authority in determining the composition of the service.

In Laredo, 94% of the population speaks Spanish as the primary language, and one in four speaks Spanish exclusively. Yet Spanish language programming has enjoyed only limited availability on over-the-air signals, and citizens have traditionally relied on cable for television in their language, a situation which continues today. As indicated in the answer to the previous question, the cost of receiving Spanish language signals on cable has now escalated to $17.00 per month.

Congress has previously recognized the potential importance of foreign language programming to operation of a cable system in the public interest in some communities. In the legislative history to Sec. 544(b)(2)(B) of the Act, which empowers franchising authorities to "enforce any requirements contained within the franchise ... for broad categories of video programming or other services", foreign language programming is cited as a specific example of what Congress intended. 1984 U.S. Code Cong. & Administrative News 4655, 4705-06 (1984). Relying in part on this legislative history, the Vermont Public Service Board has upheld the requirement of a French language channel as consistent with the First Amendment and the Cable Act when included as a condition for approval of the transfer of a cable television franchise in a community near the Canadian border. In Re Petition of Adelphia Communications Corporation and Chelsea Communications Inc., For Such Authorization as May Be Required to Own and Operate a CATV Business in the State of Vermont, State of Vermont Public Service Board, slip op. at 86-87, July 22, 1988.

3.) **Question: What other changes in the renewal provision do you feel are necessary?**

Answer: Overall, it is important to promote competition in the renewal process at the same time that a reasonable expectation of renewal is preserved for franchisees who fulfill their obligations under the Cable Act and the franchise to which they agreed to be bound. The renewal process should be expanded to allow for and encourage competing applications by would-be overbuilders, or proposals to replace the existing franchisee.

At present the renewal provision of the Act is grossly slanted in the incumbent operator's favor, thereby undermining the prospects for a competitive environment. For example, the standard of judicial review should be the customary "abuse of discretion", rather than the extraordinary de novo review to which incumbent operators are now entitled. Commercial impracticability should be limited as a defense against franchise enforcement actions, and should be required to be raised and resolved well in advance of franchise renewal time.

4.) Question: Many of the witnesses today support relaxation of the restriction on telephone ownership of cable systems. Do you agree?

Answer: This line of inquiry merits further investigation, but there are also serious pitfalls such as cross-subsidization to avoid if telephone entry is permitted.

5.) Question: Do your franchise agreements require the provision of public access channels?

Answer: Yes: two educational access channels (for use by the public schools); one religious access channel, to provide an outlet for the very high level of local interest in religious expression; one public access channel (available to the general public on a first come, first served basis as a means of promoting the public's First Amendment rights to speak and receive diverse information); and one government access channel. Four of these channels are now in operation. The educational access channels, and the governmental access channel, should be considered part of "lifeline service", particularly in Laredo where economic conditions make education paramount and public school programming must be available to many who cannot attend regular classroom instruction.

6.) Question: Have your cities encountered any difficulties with controversial or offensive programming carried on the public access channels?

Answer: No.

Senator INOUYE. Thank you very much, Mayor Ramirez.

I gather that all of you would be in favor of having the ratemaking authority and the monitoring authority at the State, county or city level. Am I correct?

Mr. PATTERSON. Yes, sir.

Mr. ALM. Yes.

Ms. HARRINGTON. [Nods affirmatively.]

Senator INOUYE. Am I also correct that you would be in favor of some provision that would either serve as a disincentive to the speculator, buy-and-sell operators, or to have some sort of restriction that would require them to hold on to their system for a given number of years? Am I correct?

Mr. JAMES. Yes.

Mr. RAMIREZ. Yes, sir.

Mr. PATTERSON. Yes.

Mr. ALM. Yes.

Ms. HARRINGTON. Yes.

Mr. RAMIREZ. To give you an example, Senator, in Laredo, before the system was sold to the current provider of cable, another potential buyer came in. Because we scrutinized him so closely as far as his service and financial resources were concerned, he backed off. He went out and bought two other systems. Six months later, he sold it at a $12 million profit and went into the savings and loan business.

So we definitely do need to do something about it, Senator.

Senator INOUYE. Is he still in that savings and loan business?

Mr. RAMIREZ. I don't know, Senator.

Senator INOUYE. Senator Gore.

Senator GORE. Thank you very much, Mr. Chairman.

These witnesses have all been so eloquent in their statements that I'm not sure we can add very much through questions. So I have only a very few for them.

I want, of course, to welcome my good friend, Eddie Patterson, here. He is a lifelong resident of Henderson. He worked in the construction industry, served as a part-time Mayor for four years, and is now the first full-time Mayor elected as Mayor of Henderson.

He has made a special effort to come here and let us know about what the real world is like and how a small town deals with cable television in its current form. I really appreciate it.

He came here the old fashioned way, Mr. Chairman. He drove the whole way with Mrs. Patterson, who is also here. We appreciate your coming.

Mayor, when Multivision came to West Tennessee, they blew into town about the middle of 1988, didn't they?

Mr. PATTERSON. Yes, sir.

Senator GORE. They bought up the franchises in 23 West Tennessee communities. Right?

Mr. PATTERSON. Yes, sir.

Senator GORE. When they came into town and bought out your cable system, did they meet with you or any of the other mayors?

Mr. PATTERSON. No, sir. We didn't know anything about it until the purchase had been complete and we got a notice of a rate increase.

Senator GORE. That's their community relations strategy.

They did send letters to their customers.

Mr. Chairman, they blamed the rate increase, they said one of the reasons for the rate increase was action by Congress of a kind that would come out of this Committee, that is, changes in the Communications Act. That's one of the reasons they cited.

They blamed that for the rate increase, didn't they?

Mr. **Patterson**. Yes, sir. It was totally blamed on Congress.

They did mail out letters to the subscribers stating that due to regulations forced on them by Congress, rates would have to increase.

Senator **Inouye**. We deregulated, that's all.

Senator **Gore**. Yes, that's right.

My reaction was that exactly when these 23 mayors contacted me to see what we had done to cause this rate increase.

I wrote a letter to the company and explained that I was a Member of the Communications Subcommittee and that I would kind of like to know what was going on here and what about these rate increases. They didn't answer my letter.

Finally, after another letter and a lot of time had passed, I did get a letter that said "Dear Subscriber."

Now, I am not a subscriber. I live in middle Tennessee. But they told me, too, that it was Congress' fault, what they had done.

In any event, six months later—six months after they had raised their rates from 45 percent to 100 percent, with declining quality of service—we finally got direct complaints to the company. The President, Christopher Connolly, claimed to know absolutely nothing about the situation.

Later on, Multivision's top official, Martin Pompadour, blamed it all on the precariousness of his financing. I quote: "The deal with GE Capital was so highly leveraged that everything was based on tight financial projections and there was no room to compensate for the unexpected." Let me translate that.

The cost of buying the cable television systems was so inflated that Multivision had to jack up their basic rates for captive customers so they could service their debt. That's not complicated. That's exactly what happened.

They just made a miscalculation, Mr. Chairman. They figured that Mayor Patterson and his colleagues in the other 22 towns would sit still and not speak up for their constituents and not try to protect their people.

But they did. They raised cain about it. They got me involved in it. They figured out, some of them, how to start their own cable systems. Of course, most of them decided that that was going to be almost impossible. But they did get a promise from the company to lower its rates.

The company hasn't kept the promise yet, of course. They are not known for keeping promises. But some of the towns have gotten lower rates.

Now, in the case of Henderson, Tennessee, Mayor Patterson is one of the only ones to get so far as having a contract with an overbuild. Now, when the overbuild began, Multivision did lower rates to try to keep the overbuild from being viable. That's basically it, isn't it?

Mr. **Patterson**. That's basically what they did. Yes, sir.

They didn't want the new company on the block to survive.

Senator **Gore**. Now, if the new company on the block decides to fold its tent, do you have anything to prevent Multivision from turning right around and jacking the rates back up again?

Mr. **Patterson**. No, sir.

Senator **Gore**. Nothing at all?

Mr. **Patterson**. Nothing at all.

Senator **Gore**. Well, Mr. Malone said in our first panel that it is highly unlikely in his opinion that overbuilds will be very common at all. Out of 8,000 or 9,000 cable systems, there are six or seven overbuilds—that's not 6,000 or 7,000, but six or seven. It is almost impossible for two companies in the same market to survive.

And so, the situation which prevails now in Henderson, coming about because of your determination, cannot be looked to nationwide as a solution to this problem.

Mr. **Patterson**. Yes, sir.

Senator **Gore**. In fact, right in your town, if the overbuild, if the new company folds, then you will be right back in the soup and Multivision will be right back raising its rates again.

I want to congratulate you on what you have done, and I want to thank all of the other witnesses who have come.

I would like it, Mr. Ramirez, if you would say hello to Judy Zafferini and her husband, Carlos.

Mr. **Ramirez**. I will do so.

We were pleased to see you a while back down in Laredo. We remember your visits very well.

Senator **Gore**. I was going to be the next President of the United States, Mr. Chairman, and I made many friends in Laredo.

Mr. **Ramirez**. Yes, sir.

Senator **Gore**. I appreciate you all very much.

Mr. **Ramirez**. Certainly I will say hello to her for you, Senator.

Senator **Gore**. And to Carlos. Thank you.

Thank you very much, Mr. Chairman.

Senator **Inouye**. Did you select the witnesses today?

Senator **Gore**. Well, you let me have a little hand in selecting one of the witnesses, Mr. Chairman, and I appreciate that.

Senator **Inouye**. I have just one further question.

We have been talking about excessive rates.

On the matter of shoddy service, Mr. Alm, how do you rate the Oceanic system there. That's the big one, isn't it?

Mr. **Alm**. Yes.

Their service is excellent. That's why we just negotiated a long renewal with them. We really don't have a problem with the company. We have a problem with the rate-making, particularly by their parent company.

On behalf of the consumers of Hawaii, I also want to thank you for scheduling these hearings. We had been expecting another rate increase, which was cancelled—coincidentally after these hearings were announced though we expect to see it again sometime in the spring. Maybe you can hold some more hearings. We'll be better off.

Senator **Inouye**. We'll have hearings every two months.

I thank you all very much. You have been extremely helpful.

The final panel consists of Mr. Gene Kimmelman, Legislative Director of Consumer Federation of America and Ms. Sharon Ingraham, Chairperson, National Federation of Local Cable Programmers. Mr. Kimmelman, welcome, sir.

STATEMENT OF GENE KIMMELMAN, LEGISLATIVE DIRECTOR, CONSUMER FEDERATION OF AMERICA.

Mr. KIMMELMAN. Thank you, Mr. Chairman. I want to thank you on behalf of the Consumer Federation for inviting us to testify today.

I want to start off by saying something unusual. I think this is the first time in my career representing consumers' interests where I do not feel inclined to come up before you and yell and scream about consumer concerns out of a sense that you have been distracted with other interests. In listening to the subcommittee this morning, I have never heard a better representation of consumer interest by elected officials raising all the most salient points of consumer concerns, interrogation of the cable industry witnesses, reflecting the need for a solution like Senator Danforth's bill, S. 1880.

Clearly the panel itself, your Subcommittee members and yourself, Mr. Chairman, have represented consumers' interests much more eloquently than I ever could. I will be very brief because of that.

I am here on behalf of the Consumer Federation to endorse Senator Danforth's legislation, which has been co-sponsored by Senator Gore, S. 1880, because we believe it would address consumers' major problems with the cable television industry. It would set the wheels in motion to bring basic cable rates down into line with market conditions. It would promote broader distribution of cable programming to rural America. And we believe this legislation would promote maximum competition to the cable industry and create incentives for improved cable service.

Now, as everyone has testified before you this morning, it is clear that legislation is necessary because competition to cable has not developed and because consumers are being overcharged.

In the early 1980s we heard a lot of talk about competition when the Cable Act was being discussed. There was supposed to be direct broadcast satellite. There was supposed to be satellite transmission, pay-per-view, pay-per-channel. None of that has developed. Instead, we have seen cable industry horizontal concentration and vertical integration into a complicated web of video ownership which controls a large portion of cable subscribers in this country and the most popular programming that the American people want to see.

The cable industry has packaged services together to maximize its profits and denied access of these packages to its potential competitors.

What does all this mean to the American consumer? Well, consumer tastes have also changed since the early 1980s, and I think the cable industry gets some credit for this. Consumers want the package of programming that cable is offering—the networks, news, information, educational and cultural programming, all wrapped together into one basic tier.

More and more consumers believe that they need this package of programming to meet their needs to receive fundamental news, information and educational programming on television. But, most importantly, with no other way of receiving this whole package of programming than over cable, because of technological limitations and because of cable's denial of full access to this programming to its potential competitors, consumers are being forced to pay whatever the cable operators want to charge them, for what consumers believe is necessary.

Now is this monopolistic? Well, many of us argue it is. But I think most importantly you should know that the cable industry itself argues that it is monopolistic. One need only look to the law suit, the antitrust law suit filed by Viacom against Time, Inc., owner of HBO and ATC, the second-largest cable operation in this country, to see allegation after allegation of anticompetitive monopolistic practices.

Is this vertical integration good for the consumer? Well, Mr. Mooney said sometimes vertical integration is good, sometimes it is bad. It seems to me, based on his statements, he is saying vertical integration is good when it is cable; it is bad when it is the telephone industry. And I think that raises questions as to whose interest his industry is really serving. We believe that vertical integration has hurt diversity of programming.

Cable is to be commended for delivering a valuable and desirable package of services to the American people. But we do not think cable is to be commended for the price gouging that has taken place since deregulation occurred.

Even using the most positive numbers, the GAO numbers the cable industry provided to you before, cable rates for basic service have risen two to three times the rate of inflation since deregulation, compared to much less, significantly less than inflation during the era of regulation.

We have heard discussion about comparisons to the consumer price index. It sounds reasonable, but when one looks at the cable industry, with the new technologies going into place, with expanding services and expanding subscribership, it is clear that cable is a declining cost industry, that the price per service and the price per subscriber is coming down.

So the rate increases that the American people have experienced have really been a ripoff, Mr. Chairman. Market analysis shows that with just half the revenue stream of the cable industry cable operators would be able to earn a reasonable profit. For consumers this would mean that cable rates could be reduced 50 percent, with appropriate regulatory tools like in S. 1880, and the American consumer would save $6 billion in their video revenue that they currently are handing over to the cable industry.

So, in conclusion, the Consumer Federation believes it is time for a mid-course correction in the Cable Act—legislation like S. 1880—to ensure that the law reflects current market conditions, so that basic cable rates can fall to an appropriate level, so that consumers denied access to the cable programming they want can receive it, and to promote maximum competition and better service quality in the video industry. Thank you.

[The statement and questions and answers follow:]

STATEMENT OF GENE KIMMELMAN, LEGISLATIVE DIRECTOR, CONSUMER FEDERATION OF AMERICA

Recent developments in the cable television market make it clear that the goals of the Cable Communications Policy Act cannot be achieved unless Congress fine-tunes the Act. Growing consumer demand for the package of video services offered by cable, coupled with increased concentration and vertical integration in the cable industry, in an environment of inadequate regulation, has resulted in excessive cable rate increases and inadequate service.

The Consumer Federation of America (CFA)[1] believes Congress must act immediately to bring cable rates and industry practices in line with today's market conditions. We therefore support the "Cable Television Consumer Protection Act of 1989," sponsored by Senator Danforth, which would ensure that cable rates are reduced to a reasonable level and promote program diversity and service quality.

THE CABLE MARKET

While Congress may have dealt with many of yesterday's problems in the 1984 Cable Act, it did not anticipate the combination of lax regulation, changing consumer demand and industry concentration that have undermined the Act's goals. More and more consumers want the package of video services that cable offers yet must pay excessive rates to a cable operator who monopolizes local markets by thwarting potential transmission and programming competition. If vigorous competition had developed, as the Cable Act envisioned, or its surrogate in monopolistic markets -- effective rate regulation -- were imposed, consumers would be paying about half of what they are charged today for cable services.

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[1] Founded in 1968, CFA is the nation's largest consumer advocacy group, composed of over 240 state and local affiliates representing consumer, senior citizen, low-income, labor, farm, public power and cooperative organizations.

Consumer Demand

Television has become the premier source of information and entertainment for the American people, and cable plays an increasingly important role in meeting viewing needs. On average, consumers watch seven to nine hours of television per day,[2] and recent surveys show that demand for cable is rising because of the attractive package of news, sports, cultural, educational, entertainment, and specialized movie programming that cable offers.[3]

As cable television becomes more fundamental to everyday life, it takes on the attributes of services consumers consider necessary to function in modern society. Despite significant rate increases, cable subscribership has been steadily growing, reflecting increased income and an inelasticity of demand similar to basic phone service.[4] With the national networks -- ABC, CBS, and NBC -- bundled into a basic cable package of services, television has catapulted far beyond newspapers and radio as the American peoples' primary source of news, and consumes a growing percentage of leisure and entertainment expenditures.[5] As a result of this strong demand for the services that cable packages together -- news, entertainment, information and sports -- consumers increasingly view cable as essential to meet their video needs.

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[2] Testimony of Gene Kimmelman, Communications Subcommittee, Committee on Commerce, Science and Transportation, U.S. Senate, June 21, 1989 at 22.

[3] Kimmelman, at 20.

Competition for Offering Video Services

Despite this healthy consumer demand for a broad package of video services, there is virtually no head-to-head competition between cable companies in local markets.[6] In addition, there is very little competition from other technologies that could offer packages of video services similar to cable, like satellite dish (TVRO) or wireless cable.

This lack of competition results from an aggressive cable industry strategy to monopolize the local video market. Many cable operators, acting in concert with affiliated owners of video programming, have engaged in vigorous anticompetitive actions to prevent head-to-head competition.

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[4] Kimmelman, at 25.

[5] Kimmelman, at 22-23.

[6] Kimmelman, at 13.

For example, many vertically integrated cable companies deny potential competitors access to consumers and programming or overcharge for and restrict the use of programming that is made available.[7] National Telecommunications and Information Administration (NTIA) data clearly demonstrate that American Television & Communications Corporation (ATC), the nation's second largest cable company, discriminates against its major rival Viacom by favoring the programming of its affiliates HBO, Cinemax, USA and Black Entertainment Network.[8] Similarly, Viacom favors the programming of its affiliates over non-affiliates.[9]

NTIA data also show that the nation's largest multiple system operator (MSO), which controls access to the largest viewing audience, Tele-Communications Inc. (TCI), exercises its market power over programmers by limiting programmers' access to TCI subscribers (i.e., TCI offers fewer programs to its subscribers than smaller cable operators, saving on the cost of programming, increasing profits and leveraging programmers into preferential arrangements for TCI).[10]

Allegations of anticompetitive cable practices are not limited to industry critics. Earlier this year, cable operator Viacom and its affiliated programmer Showtime Networks Inc. (SNI) filed an antitrust lawsuit against its largest chain of affiliated competitors -- Time, Inc., HBO, ATC and Manhattan Cable -- alleging a litany of discriminatory practices. Viacom's complaint speaks for itself:

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[7] Kimmelman, at 14.

[8] Kimmelman, at 16-17.

[9] Kimmelman, at 16-17.

[10] Kimmelman, at 18.

> This is an action to recover monetary damages and obtain injunctive relief arising out of the illegal, anticompetitive and monopolistic activities of defendants Time Incorporated ("Time"), Home Box Office, Inc. ("HBO, Inc."), American Television & Communications Corporation ("ATC") and Manhattan Cable Television, Inc. ("MCTV"). Specifically, defendants Time, HBO, Inc., ATC and MCTV have violated and continue to violate the federal antitrust laws by engaging in integrated series of predatory and exclusionary acts and strategies designed to increase the costs of their rivals, raise barriers to entry and expansion, and otherwise entrench themselves as monopolists by anticompetitive conduct, injuring the competitive process and, ultimately, consumers. Defendants' violations of the federal antitrust laws include:
>
> i) monopolizing, conspiring to monopolize, and attempting to monopolize the market for pay television programming services ...
>
> ii) monopolizing and abusing their monopoly power in certain local markets for cable television ...
>
> iii) monopolizing and abusing their monopoly power in certain local markets for cable television to gain an anticompetitive advantage for defendant HBO, Inc. market for pay television programming services ...
>
> iv) entering into contracts and coercing others to enter into contracts in the market for pay television programming services ...
>
> (v) entering into an Agreement and Plan of Merger with Warner Communications Inc., the effect of which will be to lessen competition substantially or tend to create a monopoly in the market for pay television programming services, in the supply of other cable television programming, and in certain local cable markets, to entrench their monopoly power ...

Cable operators engage in similar discriminatory practices to thwart competition from technologies that could offer a close substitute to cable's video wire. Satellite dish and wireless cable services, which have a multi-channel capacity somewhat similar to cable, have been blocked out of numerous local video markets because video programmers affiliated with cable operators limit availability of their programming.

For example, cable-affiliated owners of the most popular programming often refuse to deal with wireless cable or satellite dish service distributors, or block access to their programming by signing exclusivity arrangements with cable operators.11 Time, Inc., parent of HBO, has been in the forefront of efforts to deny satellite dish and wireless cable service providers access to the most popular movie channel.12

While the cable industry argues that over-the-air video signals, movie theatres and the movie rental (i.e., VCR) market effectively compete with cable's package of programming, this is clearly not the case. The networks, independents and movies do offer partial substitutes for cable TV, however they cannot be packaged to compete head-on with cable.

If consumers want to see their elected representatives on C-Span they must purchase cable. If they want a variety of sports, entertainment, cultural and educational programming, they must purchase cable. One can, of course, attend sporting events, go to the theatre and rent movies at substantial expense, inconvenience, incurring significant transaction costs and

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11 Kimmelman, at 15-16.

12 Kimmelman, at 15-16.

wasting time. To argue that this limited alternative to cable is effective competition is a little like arguing that bicycles offer effective competition to automobiles.

Concentration and Vertical Integration in the Cable Industry

Many of the anticompetitive practices described above have been made possible because of increased concentration and vertical integration in the cable industry. The largest cable operators, like TCI and ATC, control access to such a large segment of the viewing public that they can extract concessions (i.e., exercise monopsony power) from programmers who desperately need to reach a large audience to cover their programming costs. Similarly, companies that control supply of the most extensive and popular packages of programming, like Time, Inc. which owns HBO and Cinemax, extract concessions from all but the largest cable operators (i.e., exercise monopoly power), who rely on this "magnet" programming to attract subscribers.

A complicated web of mergers, integration and joint ventures between these two largest cable operators and owners of video programming has increased opportunities for anticompetitive activities. TCI controls between a quarter and a third of cable subscribers, and ATC has about a 15 percent market share.[13] TCI and ATC's parent Time, Inc. each own substantial shares of Cable Value Network, the Fashion Channel, Black Entertainment Network,

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[13] Kimmelman, at 6-7.

Cable News Network, Turner Broadcasting and Headline News, accounting for 47 percent of all subscribers, 23 percent of all basic service subscriptions and 67 percent of all pay services (See Exhibits 1 and 2). TCI and Time, Inc. avoid competing head-to-head in the marketplace by maintaining exclusive franchises and exclusive programming distribution.

This web of relationships enhances market power for both firms and creates huge barriers to entry for potential competitors. With two firms controlling access to so many subscribers and so much popular programming, potential competitors must be confident they can simultaneously finance entry into the cable operation market and the programming business to take on TCI and Time, Inc. -- an extremely risky business venture that has not and is not likely to occur.

Ironically, the cable industry believes its diversification into programming is good for the American people, while similar vertical integration by the telephone industry would be anticompetitive and bad public policy. The cable industry argues that by investing in "content" (i.e., programming), cable operators have expanded the quantity and quality of programming.14 However, when it comes to local telephone company entry into the video transmission and programming markets, the

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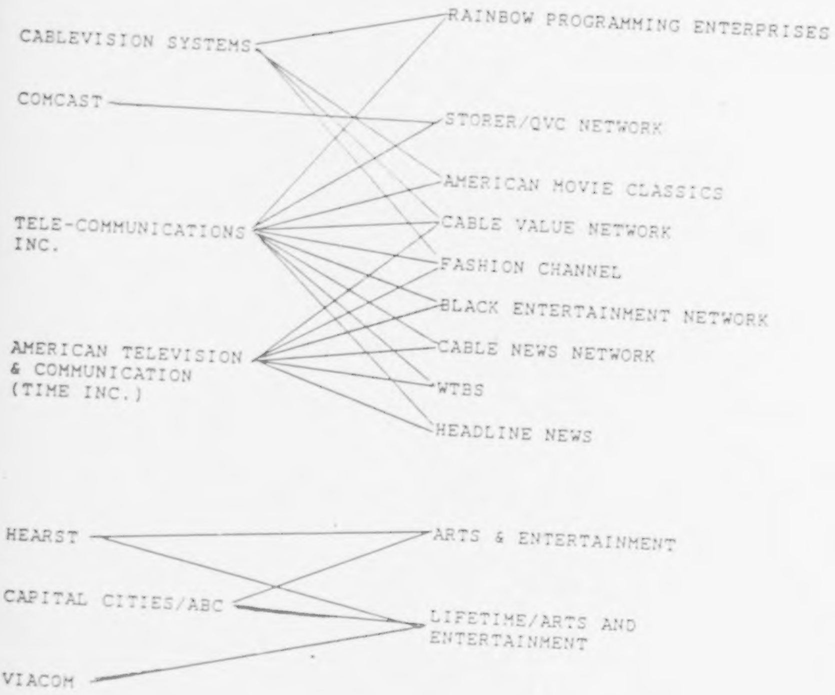
14 Statement of James R. Mooney, National Cable Television Association, Before the Subcommittee on Antitrust, Monopolies, and Business Rights of the Senate Committee on the Judiciary, April 12, 1989 at 71.

EXHIBIT 1:

JOINT VENTURES IN PROGRAMMING AMONG MAJOR CABLE INDUSTRY FIRMS


CABLEVISION SYSTEMS
COMCAST
TELE-COMMUNICATIONS INC.
AMERICAN TELEVISION & COMMUNICATION (TIME INC.)
RAINBOW PROGRAMMING ENTERPRISES
STORER/QVC NETWORK
AMERICAN MOVIE CLASSICS
CABLE VALUE NETWORK
FASHION CHANNEL
BLACK ENTERTAINMENT NETWORK
CABLE NEWS NETWORK
WTBS
HEADLINE NEWS
HEARST
CAPITAL CITIES/ABC
VIACOM
ARTS & ENTERTAINMENT
LIFETIME/ARTS AND ENTERTAINMENT

NOTES AND SOURCE: Only joint ventures are shown, wholly owned programs are not shown, but are counted in Exhibit 2 in the appropriate column. "Testimony of Jack Valenti, President of the Motion Picture Association of America," Subcommittee on Telecommunications and Finance, Energy and Commerce Committee, United States House of Representative, May 11, 1988; "Vertical Integration," in Competitive Issues in the Cable Television Industry, Subcommittee on Antitrust, Monopolies and Business Rights, Committee on the Judiciary, United States Congress, March 17, 1988, pp. 416-417.

EXHIBIT 2:

NATIONAL MARKET SHARES OF MAJOR INTERCONNECTED COMPANIES IN CABLE SYSTEMS, BASIC SERVICE AND PAY SERVICE PROGRAMMING

COMPANY	CABLE SUBSCRIBERS (000,000)	BASIC SERVICE SUBSCRIBERS (000,000)	PAY SERVICE SUBSCRIBERS (000,000)
CABLEVISION SYSTEMS	1.0	1.7	6.3
TELE-COMMUNICATIONS INC.	10.8	26.0	0
AMERICAN TELEVISION & COMMUNICATION (TIME)	4.5	0	23.9
WARNER	1.4	0	0
COMCAST	1.4	0	.2
JOINT VENTURES	2.0	186.0	10.3
TOTAL 5 COMPANIES	21.1	212.0	40.7
VIACOM	1.1	162.3	11.6
HEARST	.1	0	0
CAPITAL CITIES/ABC	0	48.8	0
JOINT VENTURES	0	65.4	0
TOTAL 3 COMPANIES	1.2	265.5	11.6
NATIONAL TOTAL	44.7	930.0	60.1
5 COMPANIES AS % OF NATIONAL TOTAL	47.2	22.7	67.4
3 COMPANIES AS % OF NATIONAL TOTAL	2.7	28.5	19.3

SOURCE: "Testimony of Jack Valenti, President of the Motion Picture Association of America," Subcommittee on Telecommunications and Finance, Energy and Commerce Committee, United States House of Representative, May 11, 1988; "Vertical Integration," in Competitive Issues in the Cable Television Industry, Subcommittee on Antitrust, Monopolies and Business Rights, Committee on the Judiciary, United States Congress, March 17, 1988, pp. 416-417.

cable industry has a slightly different perspective on vertical integration:

> In addition, to the extent that telephone companies compete in unregulated businesses that require use of or access to their monopoly telephone facilities or functions, they have incentives to discriminate against their competitors and to favor themselves in providing access to those facilities and functions.
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> . . .
>
> For example, telephone companies, if allowed to provide video programming, could still use their control of essential facilities to thwart competitors.
>
> . . .
>
> ... there are myriad ways in which telephone companies can structure their contractual relationships and everyday business dealings with other users to give themselves a competitive advantage over such users.
>
> . . .
>
> Nor is vertical integration of the telephone company's common carrier transmission facilities with the provision of video programming likely to produce efficiencies.[15]

CFA believes vertical integration in both the cable and telephone industries is dangerous to consumers' interests. Any expansion and improvement in cable programming that occurred while the cable industry became vertically integrated could be dramatically accelerated if the anticompetitive practices of vertically integrated cable companies were put to a halt.

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[15] Comments of the National Cable Television Association, Inc., In the Matter of Telephone Company - Cable Television Cross-Ownership Rules, Sections 63.54 - 63.58, CC Dkt No. 87-266 at 8,14,15,46.

Cable Rates

As a result of the lack of competition in the cable market and the Federal Communications Commission's (FCC) decision to deregulate cable pricing, basic cable rates have shot up dramatically beyond their historical level. Similar to other declining-cost industries, where per-unit costs decline as subscribership and viewership increases, the real dollar price of basic cable service declined in the era of rate regulation. In the decade prior to deregulation, basic cable rates rose only about two-thirds as much as inflation in the economy.16 In contrast, since deregulation basic rates have risen on average at least two to three times the rate of inflation.17 Cable operators attempt to camouflage these rate increases by adding new channels to their basic tier of service, forcing consumers to pay excessive rates for programming they may not purchase if it were not wrapped into the basic tier. Even for consumers who desire the new channels added to the basic tier, rate hikes have far exceeded the added cost of this new programming.

These rate increases have resulted in excess profits flowing to cable operators. Analysis of the market price for cable systems, compared to the actual cost and reasonable profits associated with cable services, demonstrates that cable systems

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[16] Mooney, at 92.

[17] Kimmelman, at 26. U.S. General Accounting Office, National Survey of Cable Television Rates and Services, GAO RCED-89-193, August 1989.

are earning large monopoly profits.18 If healthy competitive forces were disciplining the cable market, the revenue necessary to yield a reasonable profit would be less than half of what is currently paid by consumers in their cable rates.19 Since we currently lack competition in the cable market, reimposition of regulation designed to mirror competitive market forces could save consumers about $6 billion per year, reducing cable rates approximately 50 percent.20

ADDRESSING PROBLEMS IN THE CABLE INDUSTRY

CFA believes Congress must step in to stop the monopolistic pricing and anticompetitive practices of the cable industry. By reinstating regulation where comparable alternatives to cable do not exist, outlawing discrimination against potential competitors and limiting the market leverage gained from a large subscribership base, Senator Danforth's Cable Television Consumer Protection Act would help bring down cable rates and open the door to the increased competition that was originally envisioned in the Cable Act of 1984.

Until true competition for the unique package of programming available on cable develops, regulation of basic cable rates is essential to prevent price gouging. Just as Congress has a keen

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18 Kimmelman, at 30.

19 Kimmelman, at 31.

20 Kimmelman, at 1,31.

interest in providing consumers access to local news, public affairs, educational and other significant local broadcasting, CFA believes Congress has an equally strong interest in ensuring that national news, information and educational programming available only over cable is reasonably priced and affordable to the American people.

While Section 4 of Senator Danforth's bill establishes the most appropriate, fair test for when basic cable rates must be constrained, it may restrict the FCC's power too severely by preventing the Commission from developing a streamlined form of regulation. Although we have no particular preference as to where the primary locus of regulation resides, we believe it may be appropriate to direct the FCC to devise a simplified form of price regulation and more detailed functional description of basic services (e.g., local and national news, informational, cultural and educational channels) to avoid excessive complication in the regulatory process.

Sections 9 and 10 of Senator Danforth's bill would increase consumer access to video programming and promote maximum competition in the video marketplace, thereby increasing cable's incentives to improve quality of service. By breaking TCI's and ATC's lock on a large segment of the viewing public, Section 10 would prevent cable operators from exercising monopoly power against programmers. Section 9 would augment this pro-competitive result by preventing vertically integrated cable companies from discriminating against non-affiliated entities in the distribution of video programming.

Taken together, these two provisions would increase the diversity of programming available to consumers. By preventing discrimination against wireless cable and satellite dish service providers, Section 9 would increase the likelihood that consumers not wired by cable would have an opportunity to receive a broad package of video programming from non-wire technologies. This provision would also enhance the possibility to switch from cable to alternative video providers in wired communities, increasing cable's incentives to lower prices and improve quality of service. Section 10 would then reduce the largest cable operators incentives to maximize market power by limiting channel availability, opening up TCI's cable systems to broader viewing options.

CONCLUSION

CFA strongly supports Senator Danforth's Cable Television Consumer Protection Act of 1989, because we believe that Congress must step in to bring cable rates back into line with costs and promote greater competition in the cable industry. Without public limitations on cable rates (i.e., a new definition of effective competition that suits cable's monopolistic market conditions) and anti-discrimination/common carrier rules for cable operators, diversity of programming will suffer and consumers will continue to be overcharged for cable services.

CFA Consumer Federation of America

OVERSIGHT OF THE 1984 CABLE ACT

POST-HEARING QUESTIONS
FOR MR. GENE KIMMELMAN

You have indicated that there is a need to permit rate regulation. First of all, what services should be covered by this rate regulation?

> In general, all services not subject to effective competition should be rate regulated. CFA believes effective competition only exists in communities where programming comparable to cable programming is available to consumers at prices comparable to cable rates.

Would you object to the establishment of a federal rate regulatory scheme or giving the authority to the state public officials?

> CFA would support either a federal or state regulatory regime.

By what method should rates be regulated?

> CFA believes regulators should develop a simplified matrix of "limit prices" based on average costs and a reasonable return per channel offered (with variations for programming that fluctuates considerably in price). If applied on a federal level, such "limit prices" should be subject to alteration by local franchising authorities if local cable operators desire to offer a different package of regulated services, or if local cable operators can demonstrate that the "limit price" would deny them a reasonable return on appropriate investment.

If we were to establish a flat fee for a basic cable or "lifeline" service, what program services should be included in that basic tier and what should the price be?

> All services not subject to effective competition should be included in a basic tier or tiers. Prices should reflect costs plus a reasonable return, determined in the most simplified regulatory process possible (see response above).

It has been suggested that cities should have to ability to request competing applications for franchises to be considered simultaneously with the existing franchise renewal application. Why can't this occur today by the solicitation of bids for a second franchise at the time of renewal?

> As a matter of law, it appears that there is no impediment to the granting of multiple franchises.

Senator INOUYE. And do you believe that the ratemaking authority and regulating authority should be in the State, local and city level?

Mr. KIMMELMAN. Mr. Chairman, we would like to see the most simplified form of regulation implemented. We think there is an appropriate role for the Federal regulators to possibly develop a model regulatory scheme. We think that there are appropriate roles for State officials and local officials as well. We would like it to be as simple as possible.

We have no particular preference. It is clear consumers are being overcharged, and we just want to make sure that something is done about it.

Senator INOUYE. Thank you.

Senator GORE. Mr. Chairman, may I? I am going to have to go, and I wish to apologize to Miss Ingraham. I am going to review your testimony very carefully, and if you would be willing to answer some questions in writing, I would appreciate that very much.

I have just one brief question for you, Mr. Kimmelman. If it were possible to impose very tight restrictions on telephone companies of a kind that prevented cross-subsidy and avoided any increase in telephone rates as a result of their entry into the cable television business, would you under those conditions support that move?

Mr. KIMMELMAN. If those conditions could be met, Senator Gore, we would support it. It would be a positive step. But we think we are still many years away from being able to devise those kinds of protections. But if that could be done, we would be supportive.

Senator GORE. Thank you. Finally, Mr. Chairman, you have kindly kept the record open until January 15. As of January 15, I will place among the materials that I wish to include in the record an update on the story of Multivision, a list of the promises made to each community on rate reductions, and the identification of the rate as of January 15 in each of those communities so that all of my colleagues in the Senate will be able to get the latest installment of this story.

I want to serve notice to them that their promises are being watched and that the Committee will have a record of whether the rates actually go down or not.

Thank you very much, and my apologies again to you. I will look forward to seeing you tomorrow morning here.

Senator INOUYE. Thank you very much, Senator Gore.

Ms. Ingraham.

STATEMENT OF SHARON INGRAHAM, CHAIRPERSON, NATIONAL FEDERATION OF LOCAL CABLE PROGRAMMERS

Ms. INGRAHAM. Mr. Chairman, you are going to have to bear with me because I have had a cold this entire week in Washington.

Thank you very much for inviting the National Federation of Local Cable Programmers to appear before you today. As national chair, I am here to discuss a completely different area of cable than we have been hearing about so far. I am here to discuss the effect of the Cable Act on the public, educational and government access channels, or PEG access, and to address other issues of related concern to the thousands of Americans who are producing and watching this local access programming in cable system after cable system.

My organization was founded in 1976 to promote the growth and development of community access on cable. Public, educational and government channels are those channels that were set aside for community use, available to everyone in a community on a non-discriminatory basis, generally for no charge.

In 1984, the Congress recognized the growing importance of these access channels by giving cities the right to require such channels. The legislative history recognized that public access uniquely advances Congress' goals of localism, diversity and free speech. These community channels also help ensure that the operator does not have monopoly control on the electronic speech in a single community.

And everyday citizens are producing programs that have vitality, meaning and irreplaceable value to their communities.

For example, take Bob Smith, a developmentally disabled public access producer from Palatine, Illinois. He is one of many with mental or physical challenges who have learned to produce their own access programming at Project Vital.

We are told by Project Vital that as a result of this program that there are at least 30 such producers who are developmentally disabled who now have jobs in the community, who have mainstreamed lives, and one of whom has left an institution after 30 years.

Or Charlotte Wilson from Waycross, Ohio, a retired social worker who produces a weekly series focusing on the needs of housebound seniors, such a valuable service to our housebound elderly, who have few other ways of receiving programming about their community and their needs.

And how about the kids of Germantown High School in Tennessee, who produced the award-winning Germantown News and Views weekly on their cable system? Access is one of the few places where you find high quality children's television not only produced for children but produced by children. We are training an entire generation of youngsters to participate in television and use it as a communications tool.

PEG access channels have been established in nearly 2,000 cable communities and contribute over 10,000 hours a week of original programming to their home towns. That is a lot of programming. In spite of these successes, the continued existence of these precedent-setting channels is seriously threatened, and some of those threats have their roots in the Cable Act.

Of necessity, of course, I cannot go into great detail, but those are in our written comments.

Access remains unavailable to thousands more communities, at least three-quarters of the communities with cable in this country. And in others it is unavailable on the lowest service tier. We ask the Congress to *require* that access be included in every franchise, and that PEG access be included as part of any low-cost basic service tier. We are pleased to note that Senator Danforth's bill does just that.

But in other bills that have come before this body, PEG access is not even mentioned—not in must-carry, not in lifeline service proposals, and no mention so far in Teleco proposals.

Franchise fee provisions in the Act, particularly those which the operators argue mean that cash support for operating funds have to be within the five percent, often make adequate funding for PEG access and cable regulation impossible. If you throw competition in with other city budgets, then this vital community First Amendment forum is starting to come up on the losing end. We are seeing access being cut, or at least putting up a large battle.

We ask you to amend the Cable Act to allow for facilities, equipment and funding sufficient to let access continue to thrive, and make it clear that this support should not be counted as part of the franchise fee, which in fact was the situation prior to the Cable Act. In addition, we ask that you reconsider dedicating franchise fees for cable-related purposes only, primarily for local programming and for local regulation.

Franchise non-compliance and unreasonable modification requests are a serious threat to the existence of access. As you heard before from Laredo, the legal cost of regulation hampers our cities' abilities to enforce franchise provisions. For example, the outstanding public access center in Austin, Texas, and the city sapped their limited resources to fight a modification proposal that would have wiped out access funding completely and cut their channels in half.

You could help by giving our cities and towns better means to enforce franchise agreements, for example, giving them the ability to impose penalties or recovery of legal expenses in enforcement actions. You can strengthen the language which is supposed to protect local programming support from unwelcome modification requests.

Another problem is that in some communities, access has been selectively negotiated. For example, in St. Petersburg, Florida, which just went through renewal, the city chose to only have government access. You can help by clarifying the Act to ensure that all interests and groups in the community are entitled to use the access channels, as they are in most communities.

Cities and access centers who are not allowed to edit the content of the public access channels, by law, are at risk over content-based law suits. We ask that you extend to these operators of access channels the same freedom from content liability which the Cable Act has granted to cable operators.

Finally, just as you have heard today, high rates also affect access viewers by making local access programs potentially unaffordable. NFLCP joins others who feel that some measure of regulation is needed to guarantee that access is affordable as one of the key lifeline services of cable.

Our public, educational and government access centers have achieved something that is no less than remarkable. On budgets, small budgets, that would be unimaginable to a local broadcaster, we carry out training to produce local programming. We produce hundreds of hours in each community of programming, and every hour of that programming represents dozens more hours of volunteer time.

We want to ensure that any community, no matter how small, has a way to use that most powerful medium, television, to address community needs and concerns.

Where public, educational and government access gets the support is deserves—adequate funding, equipment, facilities and channels—the access center often produces more local programming than all its local broadcast centers combined.

With the changes that the NFLCP has requested you to consider, here and in our written testimony, this high level of local service and diversity of information could be brought to thousands more communities. Without your help, this community service may not survive at all.

Thank you.

[The statement and questions and answers follow:]

STATEMENT OF SHARON B. INGRAHAM, ON BEHALF OF THE NATIONAL FEDERATION OF LOCAL CABLE PROGRAMMERS

Thank you, Mr. Chairman, and members of the Subcommittee, for inviting the NFLCP to appear before you today. As National Chair, I am here to discuss the effect of the Cable Act on public, educational and government or "PEG" access and to address several other issues (including rate regulation and franchise enforcement) which are of central interest to the many thousands of people, located in almost every state, who produce access programming.

PEG access channels are cable channels set aside for community use, available to everyone on a nondiscriminatory basis, usually for no charge. U.S. News and World Report calls it "participatory television" because access makes the most important medium of mass communication available to the ordinary citizen, the underfunded non-profit organization, and the underserved minority community. As such, PEG channels make good on the First Amendment's guarantee of the right to free speech in an age when more people have television sets in their homes than running water, and provide the only effective opportunity for all citizens to contribute to the "information age."

In enacting the 1984 Cable Act, Congress recognized the importance of access and affirmed local authority to establish access requirements. The legislative history explained, eloquently and forcefully, how access uniquely advances government interests in localism, diversity and free speech, and could help ensure that the cable operator would not control all channels of electronic communication in a community. Congress hoped that communities would be able to use their local cable system to address their own needs, thus harvesting the public interest potential of cable's broadband capabilities. It was believed that by providing for access, "groups and individuals who have generally not had access to electronic media [would gain] the opportunity to become sources of information in the electronic marketplace of ideas." It was hoped that the PEG channels would "contribute to an informed citizenry by bringing local schools into the home, and by showing the public local government at work."

NFLCP, as the national organization dedicated to the growth and advancement of PEG access across the country, is pleased to report that these high hopes are being matched by tremendous achievements in communities all across the country. According to a recent article in The New York Times, nearly 2,000 access facilities are producing over 10,000 hours a week of local cable programming. In places like Columbus, Ohio; Grand Rapids, Michigan; Gresham, Oregon; and Austin, Texas; the access center produces more original programming than all the local broadcast stations combined, meeting community needs and offering diverse points of view found nowhere else on television. And, there are many other success stories:

o In Palatine, Illinois, the Little City Foundation of Chicago began a show called "Wishes and Ideas." As part of this program, people with mental and other developmental disabilities are trained to create their own programming. By allowing those facing developmental challenges to speak for themselves, "Wishes and Ideas" is able to attack traditional misconceptions which prevent the developmentally challenged from fully participating in community life. The show demonstrates the developmentally challenged are full-fledged members of the community, hardworking and productive, who have something to offer their neighbors. As a result of their work in access many previously institutionalized individuals (including, in one case, a person who had been institutionalized for 30 years) were able to obtain jobs and began to live independently in the community. The project has been so successful that it is now being transplanted to communities in New York, Illinois, Minnesota, Ohio, Maryland, Iowa and Arizona.

o In Somerville, Massachusetts, the Deaf Media Collaborative produced a two hour international teleconference on deafness-related issues for hearing-impaired viewers. The entire program was signed, and was carried in 15 communities on the public access channels.

o In Portland, Oregon, high school students produced a highly acclaimed documentary, "Kids on the Streets," in which they interviewed many of Portland's homeless youth. Interviews with social workers and government officials completed this moving program. This committee has been particularly concerned by the dearth of high-quality, non-commercial children's programming. Access users are creating high-quality children's programming (much of it produced by children themselves).

o In Waycross, Ohio, Charlotte Wilson, a retired social worker, produces "Your Turn," a one-hour weekly series focussing on the special needs of housebound senior adults. On a national basis, the AARP, a longtime supporter of public access, recently announced seed grants to encourage senior programming in St. Helens, Oregon, and Norwalk, Connecticut.

o In Nashville, Tennessee, John Furgess of the state's Department of Veteran's Affairs hosts "Vet's Point," serving Nashville's estimated 60,000 veterans. "Vet's Point" is Tennessee's only weekly television series dedicated to veteran's affairs.

o In Cupertino, California, the growing Vietnamese community can get one hour of news each week in their native language on the public access channel. This is the only programming available in Cupertino in Vietnamese. A similar program is being produced by the Vietnamese community in Houston, Texas.

I have attached for your review information about other remarkable programs that appear on PEG access channels, as well as additional information about access centers, their operations and their programming.

I have also attached a selection of letters written by volunteer producers and organizations from around the country, testifying to the special needs that access is fulfilling. I hope you will take a moment to scan the variety of access users: seniors, the League of Women Voters, veterans, ethnic minority groups, organized labor, Congressional Representatives, the Red Cross, the Boy Scouts and the Girl Scouts, churches, synagogues, and many, many thousands of average citizens, all of whom have found that access is a vital community resource. This kind of response clearly demonstrates that access programming is widely recognized as a true lifeline to the community and its concerns.

Moreover, survey after survey have shown that access channels are being watched and that the programming is valued by viewers. Professor Frank Jamison of Western Michigan University researched access viewing patterns in 78 cable markets with nearly 2.7 million subscribers. That research shows that close to 40% of cable subscribers are tuning in to government meetings, over 37% watch local arts and entertainment programs, and 31% look to public access for health and wellness information.

Unfortunately, our experience over the last five years also shows that certain portions of the Cable Act threaten the future vitality of access in every community. Consider the problems that access centers all across the country have faced:

o In Austin, Texas, home to what many consider one of the nation's model access operations, the cable operator approached the city in 1987 with a 77 point request for franchise modification under the Cable Act. The operator sought to eliminate all operating funds for access and to cut back the system's PEG access channels from eight to four, leaving only one for public use. The company went so far as to take out full page ads in the local newspaper to promote its case to the public. A retired Federal judge, brought in to hear testimony and issue an initial opinion, rejected all of the company's claims, but both the city's and the non-profit access corporation's resources were badly stretched in an effort to fend off the unsuccessful attack.

o In Dayton, Ohio, where the cable franchise is being renegotiated, dozens of community groups have testified in support of access. Yet because of the renewal provisions of the Cable Act, the City has been hampered in its effort to ensure that Dayton's well-documented access needs will continue to be met; the local operator seems unwilling to provide either additional space or funding at a level that will fully accommodate increased demand or inflation and apparently doesn't believe the Cable Act requires it to respond to demonstrated community needs in this regard.

o Earlier this year, in Nashville, Tennessee, the metro government, facing a budget squeeze, was encouraged by the Cable Act's franchise fee provisions (which place no federal restriction on how fees may be used) to redirect franchise fees earmarked by contract for public access to the General Fund. As a result, the budget for Nashville's public access operation was immediately cut by 80%. Cable subscribers and access users objected vigorously, finally securing funding for the access operation form the city budget for one year. As Endean Gerdes, Executive Director of the local Social Action Group on Aging wrote, "the issue here is every Nashvillian -- individual or agency -- losing the use of Nashville's only free and unrestricted television channel, our best opportunity for full First Amendment rights in television."

o In Massachusetts, which has an outstanding record in the number of communities with successful PEG access centers, the State recently considered legislation that would funnel one-third of the 5% franchise fee directly to the State. Because of the franchise fee provisions in the Cable Act, which may consider cash access support payments in new franchises to be part of the franchise fee, many access centers would face immediate budget cuts of over 30%. Local franchising authorities will lose the right to maintain the level of PEG access support they negotiated in local franchises under this proposal.

One of the problems you have heard about recently from other program suppliers, channel placement, applies to PEG access channels as well. In my home town of Acton, Massachusetts, for example, the public access channel was shifted when the system owner changed. The channel, which had been placed at position 19, was suddenly bumped up to channel 61. Moreover, for people who choose not to have premium pay services, the access channel is now separated from the majority of other programming by 16 channels of "snow," effectively discouraging viewership.

Access operations often suffer the ill effects of the cities' well documented problems in enforcing franchises since the Cable Act was passed. For example, in St. Paul, Minnesota, the cable company has failed to provide $230,000 worth of equipment and eight of the 10 full time staff that it promised in its franchise agreement. The company is now seeking to formally cut back on its public service commitments and to be excused from those still unperformed. At a public meeting last year in his home district, Congressman Edward Markey heard from several communities that access provisions promised in franchises were going entirely unfulfilled, in some cases for five years or more.

Moreover, in Erie, Pennsylvania, St. Paul and a number of cities in California, members of the cable industry have mounted serious legal challenges to the community's right of access. Despite Supreme Court precedent that unambiguously recognized that "[it] is the purpose of the First Amendment to preserve an uninhibited marketplace of ideas . . . rather than countenance monopolization of that market," these attacks have continued to sap cities and access operations of much needed resources; the threat of multi-million dollar damage suits discourages franchise enforcement.

Let me emphasize, these problems may be widespread, but several cable operators and many municipalities have been supportive, willing partners in the growth and development of public, educational and government access. Many operators and many governments now recognize access is a local public service that is unique to cable.

However, as indicated above, the Cable Act, as now written, does not ensure that the needs and interests of communities will be served by cable. We therefore believe the Cable Act must be modified. In addition, the Cable Act must be reevaluated in light of the many critical changes in telecommunications which have occurred since 1984 and the many which we now expect will occur in the near future. It appears that this country is moving toward the development of a broadband telecommunications network which will fundamentally alter the way in which we communicate with one another. The NFLCP is very concerned that all Americans have real opportunities to speak and to receive a diversity of information, from a diversity of sources, over that network. We think public access is essential to this goal.

Congress should take at least the following steps to resolve current Cable Act problems and to move toward an environment which will permit us to reap the fullest public interest benefits from the broadband networks of the future:

o Access channels ensure that members of the public, including citizens traditionally underserved by media, have an opportunity to speak, and an opportunity to receive diverse information from a variety of sources. Proposals for must-carry rules, rules designed to limit vertical integration, telco entry -- none of these insure that at the local level, people have real opportunities to communicate with one another. Yet in many communities, access is not available, or cannot be received on the lowest cost, basic service tier.

> Cable's potential to support outstanding local service and diversity is going untapped in thousands of communities because the Cable Act allows access channels to be required but does not mandate them.

> Congress should require that access be provided as part of every franchise. "Fallow time" rules insure that channels which are not used are not left empty. By mandating access, Congress can ensure that decisions are not made today which effectively lock the public off the cable for 15-20 years.
>
> Congress should ensure that access is treated as part of the basic, lifeline service provided by cable television. Access channels should be included as part of the lowest cost, basic service tier.
>
> Telephone company entry into the cable business -- if permitted at all -- must be conditioned so that any telephone company which provides cable service is required to set aside a complement of public channels (preferably managed by an independent, community-based non-profit organization), and is required to provide facilities, equipment and funding sufficient to support public use of those channels.

o Many communities are finding that the franchise fee provisions of the Cable Act make it difficult to insure adequate support for access in new or renewal franchises. Operators argue that any funding they provide for access must be deducted from the franchise fee. However, in most communities, franchise fees cannot adequately support a good enforcement program and an active PEG access program. There is a serious danger that access will be starved in the future (even in cities where municipal funds are dedicated to access support) unless the Cable Act is changed.

> Congress should amend Section 611 and 622 to make it clear that operators can be required to provide facilities, equipment and operating funds to support access, and to make it clear that any such support is not to be counted as part of the franchise fee.
>
> As a separate matter, Section 622 also should be modified to insure that franchise fees are used for cable related purposes, such as local programming support and franchise enforcement.

o Franchise noncompliance and unreasonable modification requests are a serious challenge to the existence of access. Communities are finding that it is very expensive and time consuming to enforce franchise provisions, and thus, many are reluctant to enforce the provisions at all.

> Congress should strengthen the position of local franchise authorities to enforce franchise provisions, by imposing penalties and allowing recovery of attorney's fees in enforcement actions. Just as importantly, Congress should encourage citizen enforcement by empowering individuals to enforce Cable Act provisions and to recover attorney's fees if the challenge is successful.
>
> The modification provisions of the Cable Ac. must be altered to discourage actions which are designed merely to delay franchise compliance. PEG access provisions for facilities, channels, equipment and funding should be clearly exempt from unwelcome attempts at modification.

o We have found that access is often most successful when it is operated by an independent, community-based non-profit group rather than the cable operator or the City. However, some operators argue that the Cable Act does not permit the City to require that access be managed by a third party.

> Congress should modify Section 611 to make it clear that Cities may require an operator to provide access services through an unaffiliated, non-profit organization.

o In some franchises, access has been selectively provided, so that some interests are guaranteed a voice on cable but access is denied the majority in the community. For example, just recently in St. Petersburg, Florida, the city arrogated to itself the right to use the cable system, but denied the citizens at large similar rights.

> Section 611 should be clarified. We think it is a good idea to have channels for public, educational and government access. It should be unlawful however, to provide for only educational or only governmental access, and exclude members of the public. It is flawed policy to reserve access for select groups.

o Cities and non-profit access corporations, which often operate the access channels, have been threatened with suits for access programming. In Cincinnati, Ohio, both the access center and the city were sued by a local resident over program content on the access channel, even though neither entity exerts any editorial control over the channel by law.

> The NFLCP joins wholeheartedly with the National League of Cities and the U.S. Conference of Mayors in urging Congress to extend the exemption from content liability now enjoyed only by cable operators to cities, access corporations and other access management entities.

o As you are very well aware, rate deregulation has allowed cable rates to sky-rocket in many communities. Many low and moderate income people find it increasingly difficult to afford cable, and thus miss the community services available on access channels.

> We join with consumer groups, cities and many in Congress who believe that cable rates should be regulated; access channels, no less than local broadcast stations and some of cable's important informational programming, should be available to everyone in the community at a reasonable cost.

NFLCP is proud of the growth and progress that access has enjoyed throughout the country. Nevertheless, we are concerned that without Congressional attention to the problems we have outlined, public, educational and government access will become an empty promise. We deeply appreciate the opportunity to come before you today to share our experiences and examine some of our challenges. NFLCP looks forward to being a continuing resource to members of this Subcommittee as you review national cable policy and shape policy that will govern emerging technology.

TO: SENATE COMMUNICATIONS SUBCOMMITTEE

DATE: JANUARY 5, 1990

RE: OVERSIGHT OF THE 1984 CABLE ACT

RESPONSES OF MS. SHARON INGRAHAM, CHAIR NATIONAL FEDERATION OF LOCAL CABLE PROGRAMMERS (NFLCP) TO POST-HEARING QUESTIONS

You have indicated that there is a need to permit rate regulation. First of all, what services should be covered by this rate regulation?

In addition to the regulatory authority that states and localities now have, they should have the authority to regulate rates for basic cable services. For these purposes, we suggest that "basic" service be defined as covering those services not available on a per channel or per program basis from the cable operator.

The NFLCP also believes that rates for access to leased access channels and the use of institutional network services for non-profit organizations should be covered. (PEG access should continue to be provided at no charge to users, as it is now in the vast majority of cases.)

The NFLCP believes that leased or "commercial" access rates need to be included because the current rate setting procedure has largely eviscerated the potential of leased access. Congress' explicit intent, "to assure that the widest possible diversity of information sources are made available to the public from cable systems," has been thwarted because the cable operator sets a rate that the prospective lessee must go to court to demonstrate is "unreasonable" if he believes it is too high. This arrangement has allowed operators to set almost any price, secure in the knowledge that the lessee has a very difficult burden and no other viable option for video distribution to the home. NFLCP believes that the potential value of leased access could be realized if rates could be controlled locally, the burden of proof were shifted off the party seeking access, and a mechanism would be put in place for reviewing rates expeditiously.

Would you object to the establishment of a Federal rate regulatory scheme or giving authority to the state public officials?

We are concerned that the establishment of a Federal rate regulatory scheme would not serve the interests of locally responsive cable policy. We believe that the likely Federal authorities would find it difficult to administer such a scheme on a national basis. As such, a Federal scheme would likely not reflect the many varied local conditions that affect costs and thus rates.

Rather than encouraging Federal intervention in local cable matters, the Federal government's most constructive role would be to restore authority to communities to ensure that cable operators meet local needs. Those needs are best understood locally, and would be best served if control were held locally. It may be appropriate for Congress to prescribe minimum procedural due process requirements, such as notice and opportunity for interested parties, including residents in the community, to participate in proceedings.

In order to more effectively facilitate that, we encourage Congress to provide authority at the Federal level for joint action among local communities facing similar cable conditions. Such joint action might include municipalities banding together to regulate jointly, consistent with state law, or simply sharing resources to study costs and rates on a regional basis.

Congress could further support and strengthen local authority if it directed the Federal Communications Commission to develop a uniform system of accounts for cable system operators to file with regulatory authorities for these purposes. (In order to preserve local flexibility, any such uniform system of accounts must be explicitly considered a 'baseline' minimum amount of information, so that if local authorities needed additional data, they would be clearly empowered to request information over and above that required to fulfil the mandated system of accounts.)

State authority is also possible, but a preferred solution would allow the "franchising authority" to assume regulatory powers. As such, states could retain those powers or delegate them to municipalities to handle.

By what method should rates be regulated?

Cost of service regulation is a possible method, but it may be too expensive for local governments to administer or for state authorities to do for every municipality. Therefore, rather than require cost of service regulation, the Congress should encourage negotiation as an alternative by affirming local authority to enforce rate guarantees contained in a franchise. Rates could thus be negotiated and regulated by contract, including contractual clauses for rate increases and timing, as the local parties agree may be necessary. Rates found to have been increased without approval should be subject to refunds.

We believe it is contrary to these purposes for Federal or state authorities to establish minimum or "automatic" rate increases or provide conditions for rate increases outside this framework.

If we were to establish a flat fee for a basic cable or "lifeline" service, what program services should be included in that basic tier and what should the price be?

Any such "lifeline" service should reflect the traditional Congressional priority on local communication and sources of information. The PEG channels are often the most important channels for local information and expression and are unavailable by any other means. As such, the NFLCP believes that any lifeline tier or service must include the PEG channels.

The NFLCP finds no evidence that the cost for providing a lifeline tier that included the PEG channels should exceed $2 to $5 per month, given the marginal cost of maintaining the system. By way of comparison, we note that Cablevision serves a major urban system, the city of Boston, with a "lifeline" plan that provides a full 52 channels for approximately $7.50.

It has been suggested that cities should have the ability to request competing applications for franchises to be considered simultaneously with the existing franchise renewal application. Why can't this occur today by the solicitation of bids for a second franchise at the time of renewal?

We do not believe the Cable Act precludes a second franchise, but it effectively prevents competition for the existing franchise at the time of renewal. More importantly, however, while soliciting such bids might be technically possible, such a proposal simply fails to recognize the economics of providing cable service.

Under current procedures, which, as a matter of practice, all but guarantee renewal to the incumbent, soliciting bids for a second franchise is inviting companies to sink tremendous capital to compete against an entrenched incumbent, who is well insulated against failure. This perhaps explains why in the many states where franchises are explicitly non-exclusive, we find almost no cases where a second operator appears. Indeed, some communities, such as Wakefield, Massachusetts, have requested competing applications and found that no other operator was willing to submit proposals.

We believe that the renewal procedures thus effectively prevent municipalities from bringing in effective competition, since it is so unlikely to get a competing or better offer to provide cable service, or ensuring that the best possible services to meet local needs are provided. Competition for the franchise at the time of renewal is necessary to establish an effective renewal process. As the Eighth Circuit pointed out in its decision in Central Telecommunications v. TCI Cablevision, 800 F.2d 711 (8th Cir. 1986), cert. denied, 480 U.S. 910 (1987), cities must have the ability to replace an incumbent franchisee with a competitor; otherwise the incumbent will remain "entrenched in its monopoly position." 800 F.2d at 717.

In addition to the lack of such competition to spur local service, the current process does not make clear the power to ensure that local needs, such as PEG access services, facilities and equipment, are met. Thus, many municipalities find themselves badly hobbled at renewal, unable to ensure that both local needs are met and important communications policy goals are served. We believe that the current renewal process must be modified to restore a balance of interests to the local franchising and renewal process.

Senator **Inouye**. Thank you.

Do you feel that the Danforth bill addresses all of your concerns on the access channels?

Ms. **Ingraham**. No, it does not. It does not address a number of the issues that we have brought up here with regard to access funding and support. We need some time to look over the bill so we can make comments.

It does provide for public, educational and governmental access to be part of any lifeline tier for service, and that we heartily commend. But a number of these areas do not seem to be mentioned.

Senator **Inouye**. Thank you. I think your suggestions deserve the most serious consideration, and I would hope that you would submit supplemental testimony in this regard.

I wish to thank you both, Mr. Kimmelman and Ms. Ingraham, for your patience in waiting this long. We have just missed our lunch hour, as you know, but I thank you.

We will recess until tomorrow morning at 8:30. We will then resume our hearings.

[Whereupon, at 1:05 p.m., the Subcommittee recessed.]

OVERSIGHT OF THE 1984 CABLE TELECOMMUNICATIONS ACT

FRIDAY, NOVEMBER 17, 1989

U.S. SENATE,
SUBCOMMITTEE ON COMMUNICATIONS,
COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION,
Washington, DC.

The subcommittee met, pursuant to notice, at 10:07 a.m., in room SR-253, Russell Senate Office Building, Hon. Albert Gore, Jr. presiding.

OPENING STATEMENT BY SENATOR GORE

Senator GORE. The committee will come to order.

I would like to welcome our witnesses and all of our guests. We had a rather extraordinary hearing yesterday, in the first day of this two-day series.

Members of the committee presented evidence on price increases by cable television systems that established a pattern undeniably clear that rates have gone up much more rapidly than was contemplated when the 1984 Act was passed.

We had several interesting statements from witnesses yesterday, including statements from a panel representing the cable industry in which the single most powerful individual in the cable industry surprised many by endorsing action by the Congress to place limits on the number of cable systems an individual company can own, and even contemplated divestiture in order to meet to such limits; endorsed congressional action to place limits on the trafficking in cable franchises; indicated that in his view the FCC has been not active enough in overseeing the activities of the cable industry; contemplated more regulation, at least, at the federal level; and identified market power and market concentration as legitimate issues for attention by the Congress, whether in the form of horizontal integration, or vertical integration.

So, it was an interesting, I think, ground-breaking hearing. A record was established that will be the predicate for action in this Congress in the next session of Congress.

Today we continue the two days of hearings. And I ask unanimous consent that the statement of Senator Inouye appear in the record.

And before we do anything else, let me recognize my colleague, the Senator from Arizona, for his statement.

OPENING STATEMENT BY SENATOR McCAIN

Senator McCAIN. Thank you, Mr. Chairman. And thank you for not only conducting these hearings, but for your long involvement in this issue of many years. And frankly, I applaud your efforts.

And I also agree with you that we will probably have some kind of legislative action in this Congress, and a lot of that will be directly attributable to your efforts.

And it is also clear, Mr. Chairman, particularly given the testimony we received yesterday, that even the cable industry itself recognizes that there are flaws in the 1984 Act. And that they are, at least, in some agreement that remedies have to be made.

We welcome Mr. Sikes here this morning—Chairman Sikes. And I would like to start out by thanking Mr. Sikes for some of the efforts you have made already concerning indecency. And we appreciate some of your efforts in decency in the whole spectrum of communications, public communications. We appreciate your efforts in that way.

Not to impede the progress of the hearing, Mr. Chairman, but I think it is important to emphasize that it is clear that despite the predictions of competition when the 1984 Cable Act was passed, the vast majority of the 9,500 cable systems in this country remained local monopolies.

Most of these local monopolies are owned by a handful of companies. This gives cable operators monopoly power over rates to subscribers, as well as control over dozens of channels.

Since deregulation rates have risen dramatically, Mr Sikes, I know you will be looking at a lot of—Chairman Sikes—you will be looking at a lot of areas. Tucson, Arizona has experienced a 64-percent increase in their cable rates this year, according to the mayor and city council of Tucson, Arizona. And that is not a unique experience, as you know.

There is a growing consensus, I believe, in this committee that legislative action is necessary. And I hope that part of your comments today will be on legislation that Senator Gore has introduced, as well as legislation that Senator Danforth and I and others have introduced just recently. We would like to get some of your comments on that.

And I would also like to hasten to add that the legislation that Senator Danforth and I have introduced is not perfect. We look to modify and to improve and have your input and that of the other witnesses in how we can reshape it.

But as I said in the beginning, I believe, there is a need for increased oversight on the part of the FCC and, indeed, some legislation to correct the unanticipated evils that have befallen the industry—certainly not the industry but the consumer as a result of the passage of the 1984 Act.

Thank you, Mr. Chairman.

Senator GORE. Thank you very much, Senator McCain. And thank you for your leadership on these issues.

[The statement referred to follows:]

OPENING STATEMENT BY SENATOR INOUYE

Today, we are here for part two of our oversight hearings on the 1984 Cable Telecommunications Act. Yesterday we heard from the cable industry, state and local governments, and consumer groups. Today, we will hear from the Chairman of the Federal Communications Commission and representatives of industries that presently compete with or would like to compete with cable.

The Chairman of the FCC, Alfred Sikes, will lead off this hearing. As head of NTIA, Mr. Sikes issued a major report on video program distribution, which included many recommendations on how to make the cable industry more competitive. He also will talk about the FCC's current activities in this area. Under the 1984 Act, the FCC is obligated to report to Congress later next year on the state of competition in the cable industry.

Mr. Sikes will be followed by three panels comprised of representatives of industries that are involved in or wish to be involved in video program distribution. The first panel will have two witnesses from the broadcast industry: Edward Fritts, President of the National Broadcasting Association; and Preston Padden, President of the Independent Television Association. Broadcasters both complement cable and compete with it. They are most concerned with cable's market power and believe there is a need to harness it.

On the second panel will be: Robert Schmidt, President, Wireless Cable Association; Robert Phillips of the National Rural Telecommunications Cooperative; and Charles Dawson of the home satellite dish organization, C–SAT. These witnesses want access to cable programming to feed their distribution networks. They have testified in past Subcommittee hearings that there needs to be some form of regulation to ensure they get access to this programming at reasonable rates.

The final panel will have: Ken Foster, President, GTE Telephone Operations; and Dean Swanson, Chairman of the United States Telephone Association. They will testify about how the telephone industry could provide video programming and why the cable-telephone prohibition should be repealed.

Senator GORE. Our first witness will be the Hon. Alfred Sikes, Chairman of the Federal Communications Commission. Chairman Sikes, as one committee member who voted against your nomination, your confirmation, when it was before the committee, let me say that I have been most impressed by your brief tenure at the Commission and grateful for the speed with which you have addressed a number of issues. And I look forward to an opportunity to working with you.

And we are delighted to have you as our lead-off witness today. Without objection, your complete prepared statement will be included in the record in full.

You are now invited to proceed as you see fit.

STATEMENT OF HON. ALFRED C. SIKES, CHAIRMAN, FEDERAL COMMUNICATIONS COMMISSION

Mr. SIKES. Thank you very much, Mr. Chairman, for your comments. And I will abbreviate my testimony, which as you indicate, will be in the record.

I appreciate this opportunity to participate in your review of cable television issues. Let me, first, review some of our fundamental policies, then discuss cable trends and, finally, outline an FCC action program and explain why we think it is needed.

American media policies have assumed that the same competition which spurs responsiveness, innovation, and fair prices will also promote what Mr. Justice Holmes called free trade in ideas.

Assuring effective competition, however, requires two things: open entry and a market environment which is conducive to competitors surviving.

Today, local cable markets are not open. The 1984 Cable Act lets localities grant monopoly franchises and also sharply limits potential competition between cable and other video transmission facilities. We believe these restrictions should be changed.

But before going further, we need to remind ourselves of the considerable accomplishments achieved by cable television. Our country enjoys the world's largest and most developed video distribution infrastructure.

And even the most strident critics of American video programming are usually placed on the defensive by the list of cable networks, such as CNN, C-Span, Disney, the Discovery Channel, Nickelodeon, and Arts and Entertainment.

At the same time, subscribers, competitors, and programmers alike have legitimate concerns. Subscribers, for example, are concerned about rates and overall service quality. Broadcasters are concerned about retransmission as well as channel positioning.

Programmers are concerned about the continuation of the cable compulsory copyright licensing system long after marketplace developments have made it obsolete.

Cable channel programmers are concerned that increasing horizontal and vertical concentration levels will hurt their ability to gain access to cable facilities and compete.

The FCC wants to ensure an effective, competitive video marketplace. We also have a statutory responsibility. Section 601 of the Cable Act specifically directs the FCC to promote competition in cable communications and minimize unnecessary regulation that would impose an undue burden on cable systems.

Today, I want to outline a number of major FCC initiatives and discuss several legislative steps as well. We believe these will further the national interest.

First, the FCC will accelerate and expand the cable industry analysis which was directed by the 1984 Cable Act. We were required to submit that analysis by October of 1990. Instead, we intend to develop a comprehensive report and submit to the Congress next July.

The appropriate public notices are now being prepared and will be released soon. We will address and report on issues including, but not limited to, indications of excessive market power, local cable service prices, horizontal and vertical integration, the likelihood of new multichannel competitors and, as I indicate, other subjects.

In conjunction with this report, Mr. Chairman, my colleagues and myself also plan to conduct field hearings outside Washington, to the extent that our resources will allow.

In addition, we plan very early next year to start, and not later than mid-year to conclude a reexamination of the current effective competition standard.

The FCC in 1985 determined that a cable system faces effective competition when the franchise market receives three or more unduplicated broadcast signals. The practical consequence was to remove most local rate regulation. We need to reexamine whether the premises for that action remain valid today.

Any price regulation, of course, should be applied to the extent that competitive marketplace forces cannot safeguard consumers' interest. If price regulation is reimposed, it is important at the same time to adopt procompetitive policies, which over time will facilitate phasing-out that regulation.

Accordingly, the FCC also plans soon to complete action on its pending inquiry regarding possible telephone company provision of video services. The FCC will shortly commence appropriate proceedings to facilitate the development of wireless cable and other multichannel video media.

We also intend to examine the alleged withholding of certain programming. Like the members of the subcommittee, we have received numerous reports that monopoly cable television systems have pressured cable programmers not to fairly license their programming to microwave and satellite competitors.

Similarly, we have received complaints that cable networks, which are wholly or partially owned and financed by major cable companies, are refusing to afford competing distribution media fair access to the programming which they need to compete.

Obviously, this is a difficult area. While we have not prejudged the outcome of this review, I want to stress the importance of this issue.

Reasonable access to programming is an essential ingredient to facilities-based competition in video services. As part of our efforts we will examine the need to recommend legislative action. Today, however, let me address some of the pressure points which are at the forefront of the current legislative debate.

To begin, I recommend that Congress amend the 1984 Cable Act to provide for each franchising authority to license two or more service providers. The law today states that a franchising authority may license one or more.

The legal monopolizing of franchise territories may be the root of many of the current problems. Requiring at least two providers would address the cause, not just the symptoms. A complementary change would be to eliminate the Cable Act's provision which precludes program distribution to the home through a nonfranchised provider.

With regard to cable concentration and vertical integration, Mr. Chairman, let me again note that the FCC intends to include this matter in a study and report.

In recent years, there has been a marked increase in cable concentration, from four firms controlling about 28 percent of subscribers in 1983 to four controlling more than 43 percent today. Many major cable program networks are also owned by dominant cable providers.

If the subcommittee intends to act on a horizontal concentration and vertical integration before our report is submitted, we believe that it should consider alternatives, however, to low ownership ceilings.

One option might be to require cable companies which attain a certain national subscribership level to make both the distribution channels and the programming in which they have an interest available on reasonable terms and conditions.

Another option might be to require cable systems with market power to offer their services on an unbundled basis. Then, subscribers would have the option of only paying for those services which they want.

Finally, Mr. Chairman, let me briefly address the issue of cable must-carry rules and related copyright concerns. As you know, there have been significant changes in FCC signal carriage regulation, especially since the courts in 1985 struck down the basic must-carry rules.

These changes have unbalanced the broadcast cable relationship and undermined the rationale of the 1976 cable copyright arrangements as well. The must-carry law, however, should apply only to cable television systems which do not face effective broadband, multichannel competition.

Congress should also link must-carry obligations to the availability of the prevailing preferential copyright regime. Linking the benefits conferred on cable under prevailing copyright arrangements with an obligation to retransmit all local signals would recognize the role which preferential copyright treatment played in cable industry development.

In broadcasting, the grant of a valuable privilege has been linked to an obligation to provide service to the public. The cable compulsory license also represents a valued privilege, as it largely exempts the industry from traditional copyright concepts and obligations.

It would be reasonable, in my judgment, to condition the exercise of that privilege on a duty to provide local broadcast signal access, especially, in view of the diversity and competition benefits which such access would further.

I might add that such an approach might also better withstand the constitutional scrutiny which is a virtual certainty in regard to all laws affecting assertions of First Amendment protection.

In conclusion, Mr. Chairman, let me summarize several of my points. First, we are accelerating our congressionally-mandated cable study. We hope the resulting report will aid Congress in its consideration of new cable legislation.

Second, we are reopening our effective competition standard as it now applies regarding the regulation of basic cable rates.

Third, we appreciate the fact that not all of our recommended measures may be administratively achievable and, where legislation is required, we look forward to working closely with the Congress to help on developing legislation.

Fourth, if Congress should proceed to pass legislation prior to our report, we urge it to select the least intrusive, most target-efficient means of accomplishing its ends.

I would be pleased to review these or other points now. Thank you very much.

[The statement and questions and answers follow:]

STATEMENT OF HON. ALFRED C. SIKES, CHAIRMAN, FEDERAL COMMUNICATIONS COMMISSION

Mr. Chairman and Members of the Subcommittee:

Thank you for this opportunity to participate in your review of cable television issues, the effectiveness of the 1984 Cable Communications Policy Act, and overall regulatory policies in this important area.

Focus on Three Matters

Today, I would like to focus chiefly on three matters. First, I want to review the fundamental principles which the Federal Communications Commission (FCC), indeed, the United States, values highly, not only in conjunction with the cable television industry, but in the video services market generally.

Second, I would like to discuss some of the important trends and developments in the cable television business in recent years, and indicate how we see those affecting our fundamental goals and principles in this area.

Third, I would like to outline the major action steps which the FCC plans to take shortly in the cable area, and to explain to the Subcommittee why we believe these measures are needed. In this regard, Mr. Chairman, I would then like to comment on some of the specific cable legislative issues which are now pending.

Ensuring Effective Competition

For more than half a century, American mass media policies have been soundly grounded on competitive principles -- and a belief that those actions which foster effective economic rivalry also yield a critical added dividend:

namely, diversity in what Mr. Justice Holmes 70 years ago described as the "free trade in ideas."[1]

Essential, however, to ensuring the level of effective competition which will eliminate the need for economic regulation -- and maximize the diversity of competing news, entertainment, and information choices -- is a market environment which is both truly open to entry and compatible with the existence of competitors.

Today, local cable television markets are not open to competition. The 1984 Cable Communications Policy Act allowed localities, in effect, to grant monopoly franchises, and also placed limits on competition between cable television and other video transmission facilities.

We believe those restrictions should be changed. But open entry policies alone may be insufficient. If a target market is monopolized, competitors will have great difficulty securing the capital needed to enter or, if they do, are not likely long to survive. Competitors and an hospitable environment, in short, are necessary and complementary ingredients.

With regard to cable television, two fundamental questions must be addressed today. The first is whether the business, as it is now structured and nominally regulated, is genuinely open to competitors -- and, do those competitors have a full and fair chance to compete? The second and related question is whether the existing concentrations of economic power which we see in certain parts of this important enterprise are compatible with attaining, or sustaining, the effective competition upon which so many of our media policies are based.

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[1] See Abrams v. United States, 250 U.S. 616, 630 (1919)(concurring opinion).

Rapid Growth and Financial Success

As we examine these questions, we need to bear in mind the very considerable accomplishments which the cable television industry has achieved, and the important contributions which it makes to the national welfare.

From its inception in the late 1940s and well into the 1960s, cable television functioned chiefly as a minor adjunct to the existing, over-the-air broadcast system. Cable television improved the quality of local TV signals and, by bringing in distant signals, expanded its subscribers' choices. But the industry was overwhelmingly concentrated in less well-populated areas -- with the exception of Manhattan, where interference made conventional TV reception difficult.

Given prevailing technological as well as economic limitations, the average cable television system then offered only 12 or fewer channels. The absence of an efficient domestic communications satellite business also sharply curtailed the number of special cable programming offerings.

But with changes in technology and in prevailing regulations, many compelled by the courts, the cable television industry grew rapidly. The advent of efficient and effective satellite relay services -- coupled with preferential copyright treatment, pole attachment rights, and protection from telephone competition -- fueled that growth. By the late 1970s, the cable television industry was adding about 300,000 new subscribers monthly, a rate of growth which was sustained and even rose, during the recessionary period in the mid-1980s.

The Cable Industry Today

Today, cable television constitutes the principal way most American homes receive television. Between 1970 and 1987, the number of cable systems grew to 8,500 with 45 million subscribers from 2,639 systems serving 4.5 million homes. The percentage of households served rose to 50.5 percent from only 7.5 percent during that time period. The latest Commerce Department statistics indicate that cable television will achieve more that 54 percent household penetration by the end of this year, and will serve over 49 million subscribers.[2] About 80 percent of our 94 million homes should be passed by a cable television system by the end of this year.

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[2] See 1989 U.S. Industrial Outlook at pp. 57-5; NTIA Telecom 2000 at pp. 542 (U.S. Dep't of Commerce, 1988).

Revenue growth has been equally impressive. In 1988, for example, cable television industry revenues were some 10 times higher than just a decade before. Basic subscription charges accounted for 57 percent of the industry's $12.8 billion in revenues. Pay services contributed 30 percent, and advertising, 11 percent, or about $1.4 billion. Commerce Department forecasts, again, estimate total 1989 revenues of about $14.5 billion, up about 14 percent.

The expansion in cable television plant and thus subscriber viewing options has been equally impressive. In 1971, for example, 95 percent of all cable systems had 12 channels or less. By 1988, more than half offered at least 30 channels. About 80 percent of all cable television subscribers, moreover, were served by systems with 30 channels or more.

Cable networks and cable-originated program options have also been an impressive growth area. Today, we have more than three dozen major, national cable networks. Most, though not all, are financially linked to one of the major cable television system owners. Industry expenditures for cable-originated programming available as part of a basic service package this year should exceed $965 million, and for basic plus pay offerings, $2.03 billion, according to industry sources.[3]

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[3] National Cable Television Association estimates.

Important to Competitiveness

These very positive cable industry developments have made a major contribution toward the unparalleled breadth and quality of video service choices currently available to the American public. Cable television demand for, and production of, programming has also strengthened our competitiveness in this important area.

In my position, questions regarding American video programming often arise. As members of the Subcommittee recognize, those questions are not always fielded by that programming's admirers. But even the most strident critics are usually placed on the defensive as I read off the list of cable television networks. Overall, there are over cable networks in existence today, representing many new voices and contributing to program diversity. Services such as Cable News Network (CNN), C-Span, Disney, the Discovery Channel, Nickelodeon, and Arts and Entertainment have developed, by virtue of expanded cable delivery systems, effective satellite communications, and the revenue which success in the video marketplace has returned.

As we review current problems and concerns, and potential solutions, it is important to keep in mind both the contribution which the cable industry has made, as well as the opportunities that lie ahead.

Reviewing the Concerns

All of us have heard the concerns of a number parties regarding the current state of competition in the cable television industry. For example,

- Many customers are concerned about the prices charged for cable service, or the service problems they have encountered.
- Both public and commercial broadcasters are concerned about the retransmission of their signals, as well as their channel positioning.
- Existing and potential competitors of cable are concerned that their access to programming has been curtailed or foreclosed altogether.
- Program suppliers are concerned that the persistence of the current compulsory copyright regime is both unfair and will undermine incentives to produce.
- Both existing and potential cable program suppliers are concerned that their ability to market their service has been affected adversely by the structure of the industry.
- Broadcasters, which must compete in local advertising markets, are concerned when their access to audiences is dependent on cable systems that also compete in those markets.

Not all of these complaints advanced by private interests may rise to the level of significant public policy concerns. But the volume and intensity of complaints does indicate that there are problems which should be addressed.

The FCC has an interest in ensuring a video services marketplace which is effectively competitive, because that has proven to be the most efficient means of safeguarding the public's interest in an economically robust and diversified media market. The FCC also has a statutory responsibility to encourage the provision of new technologies and services -- and a commercial environment that will make the fruits of innovation widely available to the American people.

Section 601 of the Communications Act, which was enacted as part of the 1984 Cable Communications Policy Act, specifically directs the FCC to --

> [A]ssure that cable communications provide and are encouraged to provide the widest possible diversity of information sources and services to the public; and,
>
> Promote competition in cable communications and minimize unnecessary regulation that would impose an undue economic burden on cable systems.[4]

AN FCC Action Program

Accordingly, today I want to outline a number of major FCC initiatives -- and discuss several complementary legislative steps -- which we believe are both consistent with our statutory responsibilities and will further the national interest.

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[4] 47 U.S.C.A. §§ 601(4), 601(6) (Supp. 1989).

Comprehensive and Accelerated Study

First, and given Congressional interest in this area, the FCC will be accelerating the comprehensive analysis of the state of the cable television industry which was directed by the 1984 Cable Act. We were required to submit that analysis by October 1990. Instead, we intend to develop a comprehensive report, and to submit it to Congress next July.

The appropriate public notices and requests for comments are now being prepared, and will be released soon. In conjunction with this accelerated, comprehensive effort, we will address and report on issues including, but not limited to --

- Indications of undesirable, excessive market power in cable television, related markets, and submarkets;
- Local cable service prices;
- The level and intensity, if any, of facilities-based competition.
- Video common carriage, or "video dial-tone" as it has come to be known.
- The degree of horizontal and vertical integration, and trends in that regard;
- Programmer discrimination, and associated leased access problems;

- The feasibility and likelihood of new, multichannel competitors, as well as both facilities-based and "resale" video services competition.

In conjunction with this accelerated, comprehensive report and analysis, Mr. Chairman, my colleagues on the FCC and myself also plan to conduct field hearings outside Washington, to the extent that our limited resources will allow. The American public has a large stake in these issues, and we want to do what we can to ensure that we provide the maximum possible opportunity for as many people as possible to offer us their comments and recommendations.

"Effective Competition" Standard

Second, we plan very early next year to start and, not later than mid-year to conclude, a reexamination of the current "effective competition" standard.

In establishing its three-signal standard in 1985, the FCC determined that a cable system faces "effective competition" whenever "the franchise market receives three or more unduplicated broadcast signals" (50 Fed. Reg. 18637 at ¶100). This standard later was modified to require three broadcast signals covering the entire franchise area.

The practical consequence of this standard was to remove most local rate regulation from cable television systems. We need to reexamine whether the premises for that action remain valid today and, if reforms are needed, what minimally intrusive, hopefully transitional steps might be appropriate.

New Video Service Competitors

Any price regulation, of course, should be applied only to the extent that competitive marketplace forces are demonstrably inadequate to safeguard customers' interests. If price regulation is to be reimposed, as a number of interest groups have urged, it is important at the same time to take steps aimed at engendering the kind of pro-entry, procompetitive policies which, over time, will facilitate phasing out any such regulation.

Accordingly, the FCC also plans soon to complete action on its pending inquiry regarding possible telephone company provision of video transmission services.

Let me note for the record, Mr. Chairman, that in the past I have said that telephone company provision of video transmission services should be on a content-neutral, "transparent," or "video dial-tone" basis at this time. Such an approach would maximize the potential for channel access on the part of programmers, and thus foster more cable service competition. I will be looking carefully at the record, however, and do not want to prejudge an outcome.

Finally, let me address some of the comments which suggest that, even absent municipal and legal barriers to competition, the economics of the video services field are such that new entry is unlikely.

As a matter of law, Mr. Chairman, the fact that the opportunities for competition in a given market may be relatively limited makes preserving those limited opportunities more, not less important. For as the Supreme Court has ruled, where economic concentration is already great, the need to preserve the possibility of independent potential entry and hence the eventuality of market deconcentration is correspondingly great.[5]

We have also seen throughout our regulation of the communications common carrier business the very positive consequences of competitors "waiting in the wings," legally and economically able to enter a given market should the entrenched incumbent charge too much, curtail the level and quality of service, or otherwise abuse a dominant market position.[6] Few developments quite so spur a firm -- even one with market power -- to perform more efficiently in customers' interests than the prospect those customers might shift to an alternative. Thus, even if the current likelihood for head-to-head competition in the video services marketplace is relatively small -- given the economics of today's technology -- we should still endeavor to capture the maximum possible benefits by removing legal or regulatory barriers.

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[5] See, e.g., United States v. Philadelphia Nat'l Bank, 374 U.S. 321, 365 & n. 42 (1963); United States v. Alcoa, 377 U.S. 271, 279 (1964)("Rome Cable").

[6] The proposed deployment of commercial international communications satellite systems separate from the INTELSAT system, for example, resulted in significant rate reductions in advance of that competition. In the 1970s, when incipient competition with the unified Bell System was sanctioned, the result was to spur rate reductions, service improvements, and accelerated product development by AT&T.

Pursuing Competitive Parity

In addition to these steps, the FCC will also shortly commence appropriate proceedings aimed at facilitating the more rapid development of "wireless cable" and other multichannel video media.

We will examine, first, whether there are unintended obstacles to achieving competitive parity built into some of our existing rules. Our rules governing the licensing of private microwave relay systems, for example, give cable television operators a preference over the multipoint multichannel distribution service (MMDS) operators against whom they compete. This appears to be an unintended obstacle, which has anticompetitive consequences. Thus, we want to reexamine this regulation, and others, to see if changes are needed.

We also intend, in this respect, to examine issues including the alleged withholding of certain programming. Like the members of the Subcommittee, we have often received reports that monopoly cable television systems were pressuring cable programmers to refuse to license their programming on reasonable request and at a reasonable price to MMDS and satellite competitors. Similarly, we have also received complaints that the cable networks which are wholly or partially owned and financed by major cable companies, are refusing to afford competing distribution media fair access to the programming which they need to compete.

Obviously, this is a difficult area. Implicit in general copyright rules is the right of program owners to control the distribution of their property. Indeed, it was in furtherance of that basic principle that the FCC some 16 months ago sanctioned the assertion of syndicated program exclusivity rights with respect to competing cable exhibition.

We do not want to get into the business of regulating program distribution -- even assuming that we might have authority to do so. By the same token, it is axiomatic that the economic power conferred by a protected monopoly position should not be used to gain unfair competitive advantage in related fields.

While we have not by any measure prejudged the outcome of this review, I want to stress the importance we accord to this issue. Reasonable access to programming is an essential ingredient to facilities-based competition in the video services field. Thus, removing legal barriers to new entry but failing to address program availability may undercut the potential value of such action.

Complementary Legislation

Cable television legislation, of course, has been proposed. Six bills are currently before this Subcommittee, and others may be drafted as a result of these hearings.[7] As part of the comprehensive cable report and other FCC initiatives which I have outlined today, we will also be examining the need, if any, for recommending legislative initiatives. Today, however, I will address some of the current "pressure points" which appear to be at the forefront of the legislative debate.

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[7] See, e.g., S. 1880 (Senator Danforth's "Cable Television Consumer Protection Act of 1989"); S. 1068 (Senator Gore's "Cable Competition Act"); S. 1698 (Senator Gore's "Satellite Television Fair Marketing Act"); S. 905

Franchising

First, I would recommend that Congress amend the 1984 Cable Act to provide for each franchising authority to license two or more service providers. The law today states that a franchising authority may license one or more providers. The legal monopolizing of franchise territories may be at the root of many of the current problems. Such an approach would have the benefit of addressing the cause of these problems, and not just the symptoms. A complementary change would be to eliminate the Cable Act's provisions which preclude programming from being distributed to the home through a non-franchised provider.

Concentration and Integration

Second, the report on video services markets which the National Telecommunications and Information Administration (NTIA) released in the summer of 1988 noted cable industry trends toward concentration of system

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(Senator Lieberman's "Cable Consumer Protection Act of 1989"); S. 168 (Senator Pressler's "Cable Television Programming Competition and Consumer Protection Act of 1989"); and S. 833 (Senator Metzenbaum's "Cable Television Subscriber Protection Act of 1989").

ownership. The report also commented on the trend toward ownership of cable programming services by the larger cable multiple system operators (MSOs).

Given the ownership pattern in the cable industry, and the large number of joint ventures, "teaming arrangements," and the like, precise statistics regarding the extent of horizontal concentration and vertical integration can sometimes prove elusive. We do know, however, that over recent years, ownership concentration in cable has markedly increased, with the top four firms in 1989 controlling systems which serve about 43 percent of all subscribers, compared to 28 percent in 1983. Similarly, over the past decade, cable system owners have acquired interests in virtually all of the major premium cable networks.

This increase in ownership concentration may reflect, in part, the possible efficiencies associated with increasing firm size. Firm size, by itself, moreover, is not necessarily anticompetitive. It may enable cable companies to bargain more on a parity with the large firms which also are found in the programming business, and to compete with large broadcast companies as well. The FCC noted in 1981 that development of large, nationwide cable companies could facilitate competition with the national television networks.

Similarly, cable system ownership of or affiliation with a national programming service, by itself, may produce benefits. It can provide a source of capital for programmers, and have the effect of expanding the public's choices.

There is, of course, extensive competition policy literature dealing with the benefits and risks of horizontal concentration and vertical integration.[8] There are both public and private antitrust safeguards that may apply when concentration and vertical integration rise to the level of a full-fledged antitrust violation.[9]

The FCC may act to address competitive concerns which may not yet have risen to the level of a full-fledged Sherman or Federal Trade Commission Act violation.[10] FCC rules governing facilities ownership and parallel Congressional actions, moreover, have also been grounded on diversity considerations, and the desirability under the Communications Act to foster the maximum number of electronic "voices."[11] As part of its comprehensive review of the industry, the FCC will be assessing whether limits on ownership of cable facilities, networks, or both are appropriate.

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[8] See, e.g., Halvorsen, An Overview of Legal and Economic Issues and the Relevance of the Department of Justice's Vertical Merger Guidelines, 52 Antitrust L.J. 49 (1983); Hibsen, Antitrust Consideration of Joint Ventures, Teaming Agreements, Co-Production, and Leader-Follower Agreements, 51 Antitrust L.J. 705 (1982); Posner, Antitrust Policy and the Supreme Court: An Analysis of Restricted Distribution, Horizontal Merger, and Potential Competition Decisions, 75 Columbia L. Rev. 282 (1975).

[9] See, e.g., ITT Corp. v. GTE Corp., 518 F.2d 913, 921 (9th Cir. 1975); Cia. Petrolera Caribe, Inc. v. Arco Caribbean, Inc., 754 F.2d 404 (1st Cir. 1985).

[10] See generally Uniform Policy As to Violation By Applicants of Laws of the United States, 16 Fed. Reg. 3187 (1951). See also United States v. FCC, 652 F.2d 72 (D.C. Cir. 1979)(en banc). Cf. Washington Mut. Sav. Bank v. FDIC, 482 F.2d 459, 464 (9th Cir. 1973).

There may be measures less intrusive than low ownership limits which would preserve the benefits of size, and any associated economies of scope or scale, while minimizing the potential for abuses. One option might be to require cable firms which attain a certain national subscribership level to make both distribution channels and programming in which they have a financial interest available on reasonable terms and conditions. Another option might be to require cable systems which have market power to offer services on an unbundled basis. Subscribers would have the option of buying packages or "tiers" of services, or purchasing only those viewing choices which they want. These approachs might correct for market distortions, while retaining the benefits of vertical integration.

If the Subcommittee intends to act on cable legislation before submission of the FCC's comprehensive report, we recommend that full consideration be given to the adoption of the least intrusive alternatives. We also recommend that any new law in this field be written to ensure regular, subsequent review. In a field such as communications, which is changing so rapidly, there is a chance that legislative or regulatory requirements will persist long after marketplace changes have rendered them obsolete. The 1984 Cable Act recognized that fact, in part, by requiring the FCC six years after enactment to conduct a review. This kind of approach should be followed here.

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[11] See, e.g., FCC v. National Citizens Comm. for Broadcasting, 436 U.S. 775, 798 (1978); Home Box Office, Inc. v. FCC, 567 F.2d 9, 40-43 (D.C. Cir. 1977). Cf. Times-Mirror Co. v. Division of Publ. Util. Control, 56 P & F Radio Reg. 2d 639 (Conn. Sup. Ct., Mar. 25, 1984).

"Must Carry" and "Compulsory License"

The FCC for 20 years applied rules which required cable television systems to carry all local or significantly viewed broadcast stations, up to the capacity of the cable system. Chiefly because cable systems were obliged to retransmit broadcast programming -- and a small, disaggregated industry was deemed to lack bargaining power -- Congress in 1976 accorded the industry special copyright treatment. Cable was given a statutory "compulsory license" to retransmit both local and "distant" broadcast signals, according to FCC rules. In return, the industry was allowed to pay administratively set, not market-determined, copyright royalty fees.[12]

The FCC in 1979 and 1980, however, rescinded many of its cable "distant" signal carriage and associated rules.[13] In 1985, furthermore, the FCC's longstanding "must carry" rules were overturned, as were the new rules that the FCC subsequently sought to order.[14]

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[12] See generally Geller & Lampert, Cable, Content Regulation, and the First Amendment, 32 Catholic U.L. Rev. 603 (1983); Note, FCC Regulation of Cable Television, 54 N.Y.U.L. Rev. 204 (1979).

[13] See generally Malrite TV of New York v. FCC, 652 F.2d 1140 (2d Cir. 1981)(and citations therein).

These actions -- coupled with the rapid growth of the industry -- have unbalanced the original cable copyright compromise which Congress struck in 1976. They have also created considerable turmoil, as independent television and public broadcasting stations in particular have sought to secure, through private agreement, the signal carriage rights which FCC regulations previously guaranteed.

It is conceivable that cable must-carry rules might yet be sustained, if, for example, the Commission could develop a record showing such rules are essential to maintain competition in local video distribution and advertising markets, or to implement Congressional spending decisions regarding the availability of taxpayer-supported public broadcasting services. Assembling such a record, however, would undoubtedly prove a formidable undertaking. Even then, it is unclear that any new FCC rules could pass judicial muster, especially given the breadth of the First Amendment rights which the courts have conferred in this field.

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[14] See Quincy Cable TV, Inc. v. FCC, 768 F.2d 1434 (D.C. Cir. 1985); Century Communications Corp. v. FCC, 835 F.2d 292 (D.C. Cir. 1987), clarified, 837 F.2d 517 (D.C. Cir. 1988).

If Congress seeks to enact "must carry" legislation, however, that obligation should be placed only on cable television systems which do not face effective broadband, multichannel competition. Congress should also link "must carry" obligations to the availability of the prevailing preferential copyright regime. In this regard, Mr. Chairman, I note that the FCC only six months ago concluded that private copyright negotiations and arrangements would better serve the public, and thus recommended that Congress eliminate the compulsory license for cable retransmission of both local and distant broadcast signals.[15]

In general, a cable system which is not subject to a local signal "must carry" duty should be obliged to bargain in the programming marketplace, as do all other commercial media operations. If that cable system seeks to avail itself of the statutory compulsory license to retransmit either local or non-local broadcast signals, however, it should, by availing itself of that privilege, trigger an obligation to provide full access to all local broadcast stations.

Linking the benefits conferred on cable under prevailing copyright arrangements with an obligation to retransmit all local signals would recognize the role which preferential copyright treatment played in cable industry development.

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[15] See FCC Report No. DC-1423 (rel. May 30, 1989).

In broadcasting, the grant of a valuable privilege has been linked to an obligation to provide service to the public. The cable compulsory license also represents a valued privilege, as it largely exempts the industry from traditional copyright concepts and obligations. It would be reasonable, in my judgment, to condition the exercise of that privilege on a duty to provide local broadcast signal access, especially in view of the diversity and competition benefits which such access would further. I might add that such an approach might also better withstand the constitutional scrutiny which is a virtual certainty in regard to all laws affecting assertions of First Amendment protection.

Conclusion

In conclusion, Mr. Chairman, let me summarize several of my points:

- First, we are accelerating our Congressionally mandated cable study, and will address many of the issues which have been -- and will be -- raised at these hearings. Field hearings will be conducted, and we hope that the resulting report will aid Congress in its consideration of new cable legislation.
- Second, we are reopening our "effective competition" standard as it now applies regarding the regulation of basic cable rates;
- Third, we appreciate the fact that not all of our recommended measures may be administratively achievable. Appropriate legislation, as indicated, may be needed. Where that is required, we stand ready to work affirmatively with Congress.
- Fourth, if Congress should proceed to pass legislation prior to our report, we strongly urge it to select the least intrusive, most "target-efficient" means of accomplishing its ends. In lieu of low ownership ceilings, for example, program and channel access obligations might better be imposed.

I would be pleased to review these or other of the points which are discussed in my statement.

QUESTIONS OF SENATOR INOUYE AND THE ANSWERS THERETO

Question: One of the concerns that was raised by representatives of the city governments was whether the FCC's technical standards for cable are outdated? When was the last time the FCC updated or reviewed those standards and have there been any substantive changes in the last decade?

Answer: The Commission's present technical standards/guidelines relating to television reception quality are essentially those adopted in 1972 as part of the Cable Television Report and Order, 36 FCC 2d 141 (1972). Recognizing that these standards might be subject to additional refinement, the Commission created the Cable Television Technical Advisory Committee to recommend any necessary changes in the standards to the Commission. Representatives of municipal regulatory authorities, public interest groups, broadcasters, and the cable television industry participated in the work of this Committee. Its final report was submitted to the Commission in 1975 and some changes based on its work were implemented in 1976. Report and Order in 20765, 64 FCC 2d 743 (1977). Additional minor changes to the rules were adopted in 1985. Report and Order in MM Docket 85-38, 102 FCC 2d 1372 (1985). These standards, as enforced by the Commission between 1972 and 1985 and as used as guidelines by franchising authorities after 1985, were intended to assure that cable subscribers at the worst locations on cable systems would receive acceptable picture quality and that other subscribers, closer to systems' central signal processing equipment, would receive better quality service.

Although there have been significant improvements in cable signal television distribution technology since the adoption of these rules, the basic NTSC television standards controlling both cable and broadcast picture and sound quality have been changed in the interim only to accommodate the addition of stereophonic sound. It should be noted that these technical standards do not cover cable signal leakage, which is subject to control by other Commission rules, or facilities placement or facility requirements (e.g. channel capacity) that are subject to local regulation through the franchising process in accordance with Section 624(2)(A) of the Cable Communications Policy Act of 1984.

Municipal regulatory authorities have expressed some general concerns with respect to the existing standards, although no specific proposals for change have been received. A proceeding is in progress considering how the Commission should treat technical standards issues with respect to Class II (non-encoded, non-broadcast television), III (nonvideo communications and encoded video), and IV (two way interactive capability) channels. Further Notice of Proposed Rule Making in MM Docket 85-38, 3 FCC 2d 5966 (1988).

Question: Cable systems pay to carry all program services, even advertiser supported program services, except for over-the-air broadcast services. Should cable pay to carry local television signals?

Answer: This matter is related to the general question of how the compulsory copyright license provisions of the Copyright Act should function with respect to the retransmission of local broadcast signals. The Commission has expressed its view that the compulsory copyright law provisions of the Copyright Act should be amended to eliminate the compulsory license for both local and distant signals. Although such a change in the law would not by itself guarantee payment for the carriage of local signals, it would permit local television broadcasters to enter into contractual arrangements with cable operators concerning carriage and no signal could be carried without the consent of the station licensee. Full copyright liability would thus permit broadcasters to acquire and control the distribution of the programming they broadcast in a far more balanced competitive environment than that which now exists between broadcast stations and cable services. Cable operators would compensate broadcasters for the retransmission of their signals in direct relation to the value viewers place on the signals as they do for the other video services they carry.

Senator **Gore**. Well, we certainly welcome that impressive statement. Thank you for getting us off to a good start today.

Before we go to questions, let me inquire if Senator Gorton might have an opening comment.

Senator **Gorton**. No, my opening statement yesterday applies today as well, Mr. Chairman. Thank you.

Senator **Gore**. Senator Exon.

Senator **Exon**. No opening statements.

Senator **Gore**. Let me ask just a couple of questions first, Mr. Sikes.

We heard testimony yesterday that an overbuild is a rare exception not because of the language of the law, but because of the economics flowing out of the technology. Out of some 9,000 systems, there are six or seven overbuilds.

And in at least one of the situations where an overbuild is taking place, the incumbent franchisee is aggressively cutting rates in order to dry up the flow of capital to the overbuilding competitor.

I wonder how much relief would actually come from encouraging localities to license two or more cable companies?

Mr. **Sikes**. I think it is hard to predict. I certainly have heard arguments on both sides as to whether the provision of video by cable is or is not a natural monopoly.

I know that as long as municipal laws exist which preclude additional franchisees, as long as the Cable Act provision exists which precludes programmers from going through other than franchised providers, that we are not going to really test that proposition.

Additionally, I think, there are alternatives to what are pejoratively called overbuilds. One would be a multichannel microwave provider. And, I have specifically asked both our Common Carrier and Mass Media Bureaus to look into facilitating the aggregation of channels, which would provide a better opportunity for microwave providers.

We currently have some 1,175 applicants or providers. I must tell you, however, that providers are many fewer than the applicants, who are interested in this kind of competitive service.

There are problems relating to how many channels they can put together. We are looking at trying to relieve that problem.

And secondly, as you have noted in proposed legislation, and as I noted in my testimony, there are frequently problems in attracting the kind of programming necessary to be competitive.

Finally, and we will cite just in passing that the telephone company—or companies, I should say—present a possible third competitive alternative.

Senator **Gore**. I hope that you noted yesterday the statements by Mr. Malone that in his view the FCC has been too timid in exercising oversight of the cable industry.

I am paraphrasing only slightly. That was the clear message. And there is a feeling in the MSO community that a lot of the current problems might have been avoided if the FCC had been more aggressive in exercising the power which exists even in current law.

I will not ask you to comment on that. But I hope you recognize a green light when you see it flashing before you.

Mr. SIKES. I would like to comment on that, because I think his statement is fundamentally disingenuous.

I have reviewed, since hearing of that statement—and obviously I am new at the Commission, so I do not have the personal institutional knowledge—but I have reviewed legal filings where the largest MSOs maintained that the Commission lacked jurisdiction under the Communications Act of 1984 to promulgate, for example, cable multiple ownership rules.

And of course, it is the concentration of power question that is fundamental to many of the ills that are faced today.

Senator GORE. Do you agree that it would be a good idea to impose constraints on cable trafficking?

Mr. SIKES. I would agree to include that, because it is not currently on the list for the study and the report to the Congress. I do not have an immediate reaction to it. I generally think that placing restrictions on alienating property rights is not something that should readily be done. Perhaps there are instances here, however, where that would be justified.

Senator GORE. Well, the head of the cable industry association said it is almost impossible to argue against imposing limits on trafficking.

And, Mr. Malone and I think the other cable witness yesterday also testified in favor of such limits. And the situation is where you have a monopoly franchise and you have a cable operator that gets to know the community and they provide service, then somebody comes in with borrowed money, buys it up, sells it six months later at an inflated price and jacks up the rates in the meantime to cover the debt service. That is inimicable to the kind of quality service that we all hope can take place in the communications industry.

Mr. SIKES. Well, let me comment on two aspects of that. I think that from what I understand of the testimony yesterday by the cable industry, you are seeing what is so frequently played out with the commercial evolution of industries in America.

An industry begins with certain benefits conferred upon it by the Government, in order to help it to develop. It reaches certain concentration levels, and then it rushes in seeking regulation, believing that the bargain will preclude new competition.

My preference is for new competition. Now, with respect to trafficking, I know of municipalities that would have liked to have had current cable owners sell their systems, in order to facilitate, new cable providers.

But I do believe that is a serious question and would certainly agree to include it in our study.

Senator GORE. Well, I thought Mr. Malone had an interesting suggestion when he advised us to consider as an alternative to a strict limit on the number of years it had to be held to rather instead preserve liquidity by imposing financial penalties that were proportionate to the length of time that the system was held.

Now, let me ask just one more brief set of questions on satellite dishes.

We heard yesterday, I presented the case, and it was undisputed by the owner of the service, that TBS, just to take one example, is sold for 10 cents per customer per month to small cable systems—

wholesale rate; sold for significantly less than that to the large systems, as low as 2 cents per customer per month. The wholesale price charged to the national rural electric consortium for distribution to satellite dish owners is not 2 cents a month, not 10 cents a month, but 90 cents per customer per month.

This is in keeping with a pattern that has seen cable programmers refuse to sell to satellite dish owners except through cable companies, where large mark-ups occur. And of course, the industry has an incentive to stifle the development of a technological competitor.

Political pressure was applied by the Congress to open up at least one outlet for rural customers that have no chance of getting cable television. The rural electric co-ops formed this entity, they were briefly supportive of the cable industry after the enthusiasm accompanying the announcement of the new venture.

But the head of it came to testify and said it has been a failure because of one simple reason. The cable programmers have stonewalled us. They have given us a small trickle of programming, and the wholesale rates have been 441 percent higher than the wholesale rates charged to cable systems for the same programming.

And here you have two technologies, one of them sees the capital investment made by the distributor, the other sees the capital investment made by the customer. Because of economic control over the source of programs, there is an artificial distortion in the price charged to the ultimate customer.

And they have the audacity to argue that it is much cheaper for the distributor to get it to the customer where the distributor makes the capital investment.

It is absurd and ridiculous on its face, but they come and seek to make that argument with a straight face. I do not think it is credible.

I heard in your statement an awareness of the fundamental injustice that is taking place here. Can you convince me that I was hearing correctly? Are you prepared to really look seriously at the FCC attempting to solve this problem?

Mr. SIKES. Well, I do not know specifically what our authorities might be. I know that under the Satellite Home Viewers Act of 1988 that we—and I believe that you were the principal sponsor of that—we have opened three proceedings. One deals with the discrimination in the distribution of programming. That report is due by year-end. I am aware that the proceeding has now established a record, that that record is being summarized. Draft findings, conclusions, recommendations are being prepared.

I, of course, work with my colleagues on the Commission. So, I hesitate to be definitive beyond telling you that by year's end, we will conclude that study and make a report to Congress.

Senator GORE. Good. Thank you.

Senator McCain.

Senator MCCAIN. Thank you, Mr. Chairman.

Mr. Chairman, let us talk about for a minute about vertical integration. I noted Tuesday an article in the "Wall Street Journal", the MGM-UA bid being planned by Telecommunications, Inc., TCI.

We know about the Time-Warner merger. Should that be a matter of concern to all of us? This very significant recent increase in vertical integration concentration?

Mr. SIKES. Well, yes, I think, it should be of concern. But I think we have got to be pretty careful.

As you look at the number of valuable cable networks that have been supported by large distributors, it is quite clear that there have been benefits of vertical integration in the cable industry.

Certainly, it has occurred with some of the most valuable networks. They have used the revenue streams from the distribution side to expand the programming. And, I know that when Time-Warner established publicly its rationale for merging, again, there were synergies outlined that could be enjoyed ultimately by the consumers domestically and give that company advantages internationally.

Now, having said that, there is clearly the potential in this area for excessive concentration, excessive integration. That is noted in the broadcast ownership limits. Obviously, the Department of Justice has responsibilities in this area. Because, again, as Justice Holmes commented, we are dealing in the free trade of ideas, I think, it is an especially sensitive area for the Government to be concerned about power concentration.

Senator MCCAIN. But have not some of these mergers entailed assumption of larger and larger amounts of debt? Rather than an increase in capability, increased programming, in fact, cause rates—subscriber rates to have to go up to pay off these enormous debts that are incurred in conjunction with this?

Mr. SIKES. I have obviously read, I mean, I can only give you anecdotal reaction. I have not specifically investigated the debt structure of these deals.

Senator MCCAIN. Is it not true that you have evidence that, at least, that the cost for the sale of franchises, which seems to be in a high state of activity has gone up dramatically? Just over the past few years we have seen sales of cable franchises go from a few million dollars to over $100 million, in some cases.

Have you seen that?

Mr. SIKES. I think the monopoly position that the cable providers have enjoyed has inflated dramatically the per subscriber value.

I am told that maybe a national average per subscriber for putting in the system is about $400, and these franchises are trading something in excess of $2,000 per subscriber. So, it strikes me that is kind of the premium the market places on having that monopoly position.

Senator MCCAIN. So, if a monopoly is sold at a higher price to another purchaser, the only way that that purchaser gets his money back or makes a profit is to increase rates to the subscriber.

Does that not concern you?

Mr. SIKES. Well, I do not think that is the only way. I mean, I could certainly conceive of enhanced programming services in other ways.

Senator MCCAIN. But we have seen as a—have we not seen—let me put it a different way. Have we not seen as a result of some of the sales of these franchises at dramatically increased, some would say inflated, prices that we have seen within a short period of time a significant increase of the rates to the subscriber following almost immediately?

Mr. SIKES. I would not dispute that for one minute. I mean, again, I have been at the Commission a fairly short period of time. We have not aggregated data in the area that you are discussing.

So, I am hesitant to state something empirically. But, I came out of business, and I am aware of the pressures to pay off debt, and the approaches one takes to create the revenue stream to accomplish debt retirement.

Senator MCCAIN. Well, let me ask, when we talk about the—and I agree with it that you suggest that Congress or the FCC require that each franchising authority license two or more service providers.

What do you think the realistic chances of that actually happening are? Because one would envision one cable on one side of the street and one on the other. Do you envision that that would really have an impact on the competitiveness?

Mr. SIKES. I think it would have an impact on the competitiveness. First of all, I think, the threat—and I do not think it is a completely hollow threat—would have initially some impact.

Secondly, I would hope the FCC can act to facilitate microwave, so-called wireless cable, as a competitive alternative, which does not carry with it the investment costs. And of course, we have got the telephone——

Senator MCCAIN. Could I interrupt on that one?

Mr. SIKES. Yes, sir.

Senator MCCAIN. Is it not true that there is a—in the view of many—a long regulatory delay for these wireless carriers at this time? And that, of course, falls on your doorstep.

Mr. SIKES. Absolutely. And, I have instructed that that regulatory delay to the extent humanly possible come to an end.

Senator MCCAIN. And you were about to mention the telcos. How do you feel about allowing them some form of entry?

Mr. SIKES. I think they should be allowed to enter. I go back to the Cable Act of 1984, which says that programming can only be distributed through the franchisees. I think that provision should be eliminated.

Senator MCCAIN. Should there be any restriction, in your view, on the participation of the telcos?

Mr. SIKES. I have recommended that they be allowed the transport and what are sometimes called the ancillary services: aggregation, billing, collection, services like that, which also provide profit potential.

This was recommended in a report released by NTIA several years ago. In the meantime, I find myself at the FCC with an open docket on this matter, which in my testimony I indicated we were going to again bring to a conclusion as swiftly as we can. So, I hesitate to prejudge specifically what the Commission might recommend.

Senator MCCAIN. So, you are basically in agreement that both regulatory and perhaps legislative action is necessary very soon?

Mr. SIKES. Yes.

Senator MCCAIN. Well, finally, could I ask, if you have had a chance to study either Senator Gore's bill, or Senator Danforth's and my legislation and if there is anything that you would particularly like to comment on that you are particularly impressed by or particularly unimpressed by?

Mr. SIKES. Well, I have obviously, as you would expect, looked at those bills in preparation for these hearings. Yesterday at the FCC we had an en banc hearing on the state of AM. Earlier this week, I found myself in Boston at the National Association of Regulatory Utilities Commissioners' meeting for two days.

So, I have really not had a chance to look as comprehensively or think as clearly as I would prefer before commenting on the bill.

I think in many respects Senator Gore's bill, Senator Danforth and your bill are valuable and are in most respects quite constructive.

I have got a little bit of concern about what seems to me to be perhaps an underwriting of municipal empowerment. I think it is important that we remember that the municipalities, as Congress noted in the Cable Act of 1984, restrained significantly the development of cable, frequently extracted a variety of revenue promises——

Senator MCCAIN. Extorted, I believe.

Mr. SIKES. Yes. And so, I just think that, as we go through this, it is important, as some regulation is re-established that we think about what jurisdiction is perhaps best able to do that.

Senator MCCAIN. I agree with your point. And we would certainly not want to return to some of the abuses that we saw in the past, which frankly were a prime motivator behind the 1984 Act. Perhaps we can learn some lessons from that.

Thank you, Mr. Chairman.

Senator GORE. I think the cable witnesses, again, were good yesterday in suggesting that to the extent we give power back to localities, it be accompanied by some Federal guidelines to prevent the return of such abuses as were noted in the 1984 Act report.

Senator Gorton.

Senator GORTON. I noted in your statement that a part of your study leading up to next July is a re-examination of the definition of effective competition.

Personally, I think, that is central to this debate. Recognizing that you have only started down that road, and that you have not held this job very long, can you, at least, give us any insight into your initial personal views on that phrase? On the adequacy or inadequacy of the present definition and on what we should do if we decide to take that up as a part of any statutory change?

More than anything else, I search for a definition of effective competition. Believing that effective competition is more likely to solve more of the problems with which we are faced than any other single approach.

Can you help us at this early stage?

Mr. SIKES. Well, first of all I am not going to include this in the study that we are doing or the report to Congress in July.

We are going to initiate a separate notice of proposed rulemaking, which is, in Commission parliance, a much more decisive action and promise to conclude the ultimate rulemaking by mid-year of next year.

I hesitate, Senator—because we go through appropriately a full measure of due process, and I then effectively work through and with the Commission—to prejudge this matter.

But central to initiating this notice of proposed rulemaking is a strong view that the current definition of effective competition is not valid any longer.

Secondly, I think, the Congress can act effectively in this area. Whether it feels it must act after the FCC defines effective competition, I will leave to another time. But again, going back to the Cable Act of 1984, I think removing the phrase "one or more" and making it "two or more franchises" locally, and removing the preclusion of programming coming in through a nonfranchised provider, I think those would both be really effective in stimulating effective competition.

Senator GORTON. In that connection, you are perfectly well aware that there is, at least, some likelihood and a great deal of sentiment on this committee for reporting a bill on the subject of cable television.

Obviously, if we do so with any serious hope that it will become law during this Congress, we are going to have to report that bill before next July.

Is the Commission because of the study and because of the rule making precluded from helping us in this definition and in a number of other of these policy areas? Will we, of necessity, have to fly blind or fly with no more than a relatively generalized outline you have given us here today?

Mr. SIKES. No, the Commission will be happy to work with the subcommittee, the individual Senators that are interested, and their staffs.

Senator GORTON. Thank you. Thank you, Mr. Chairman.

Senator GORE. Senator Exon.

Senator EXON. Mr. Chairman, thank you very much.

Chairman Sikes, welcome, we are delighted to have you here this morning.

Mr. Chairman, in the interest of time, and we have a good attendance here this morning, I am going to just touch briefly on two matters: the exclusivity rules that take effect on January 1, that the Chairman is very familiar with, and also the matter of competitive choice that I have been pushing in this area for some time.

I want to start off by saying, Mr. Sikes, that I would hope that the new Federal Communications Commission could solve some of these problems, so that we do not have to pass legislation.

I simply say that legislation is likely to follow, unless we can have better understanding to do a better job in this whole complicated area than we have done in the past.

I believe that the people of Nebraska, for example, are willing to pay their fair share of the cost for having the advantage of cable television. But I would simply point out that since deregulation, or based on 1986 basic rate and 1989 basic rate, for example, the following cities in Nebraska have had substantial increases in that basic rate: Albion, plus 76 percent; Grand Island, plus 111 percent; Hastings, plus 124 percent; Kearney, 99 percent; Lincoln, 25 percent; MacCook, 88 percent; North Platt, 55 percent; Omaha, 41 percent; and Scottsbluff, 73 percent.

That is a very dramatic increase. I do not believe that people object, though, again to paying a reasonable fee if they get basically what they want.

Now, first I would like to suggest on the idea that I have been pushing for some time: that if the cable television industry as a whole wishes to take some of the steam out of the charge that they are a monopoly, then, it would seem to me that the cable television should be leading the way to some type of a competitive choice.

And I would like to know what you think of the idea. This idea, which I have raised in hearings previously, in effect, would simply require that the cable wiring becomes, in essence, a common carrier wire, much like the basic phone line now for long distance companies.

Or, in other words, if I live in Lincoln, Nebraska and I am not satisfied with the programming that I receive on the local monopoly, then, I would have a choice of saying, well, I want Cox cable out of Omaha or some other cable.

I understand that that is technically feasible. And it would seem to me that that would be a good move for the cable industry to give more choices.

What do you think of the concept?

Mr. SIKES. Let me comment, and perhaps I do not completely understand it. So do not hesitate to elaborate if my answers seem unresponsive.

First of all, at this juncture, at least, I do not support making cable a common carrier in, say, the same way that telephone companies are common carriers. Obviously with——

Senator EXON. Well, wait a minute. You are off-track. And maybe that was a poor choice of words.

What I am simply saying is that under the existing arrangement in Lincoln, NE, for example, where there is one cable television company that own one wire that goes into my home and all others, I am simply saying that I wish that that cable company and other cable companies around the United States would through technical means, that I understand is available, give me a choice.

So, that if I do not like the programming offered by the Lincoln company, I could say to them, I want a choice. I will pay you the same fee, but I want the choice of Cox Cable, or some other cable. So that I would have—there would be some competition and, therefore, would be competition with regard to the quality of programming that is being advanced.

Mr. SIKES. I think that is an interesting thought. I honestly have given not a great deal of thought to it, other than, as I mentioned in my testimony, the possibility of unbundled services as being one approach in this difficult area.

I would guess that if there is a Cox Cable franchise close to, say Omaha, that it would not cost a great deal of money to transport that. And have that as a——

Senator EXON. Option. Right.

Mr. SIKES. As an option. But I frankly do not know how the technology would work on that. And I would say this, Senator. We would be happy to, if you would like, look into the implications of that.

Senator EXON. Thank you, Mr. Chairman. I would very much appreciate your doing that. And I think if we could explore that a little bit more, it might be one of the best things that we could do for both the consuming public and the cable television industry. Everybody might be happy.

If I might turn to the second question, the exclusivity matter. Mr. Chairman, I would like to enter into the record, by reference [1], at this time, newspaper articles from the Fremont Guiding Tribune and two items from the Scottsbluff Star Herald with regard to the concerns that have been expressed to our office by those living in those particular areas.

The point is simply this, that as you know on January 1 the new syndicated exclusivity rules go into effect. These new rules have been the topic of more consistent contacts—constituent contacts to my office in Scottsbluff than any other topic.

The rules prohibit cable companies from showing syndicated programs on imported stations, if the same programs are shown on local broadcasting stations.

In Scottsbluff, Nebraska, the cable system included Denver TV stations, for example. In Fremont, Nebraska, for another example, it includes a Lincoln station. I have been told by area citizens that due to these new rules much of the Denver programming will get dropped in the Scottsbluff area, and in Fremont, the Lincoln station would get dropped entirely, because of the so-called duplication.

Many of my constituents are very upset about this. What is your view for the need for new syndicated exclusivity rules? And will you, as a commission, be reviewing those in the near future?

Mr. SIKES. I support syndicated exclusivity. I believe in the right of the broadcasters to contract for exclusivity. I know that as a broadcaster, if I could not get exclusivity, it meant that my audience potential was reduced. My advertising potential was reduced.

It would be my suggestion that the cable company which typically is stimulating these complaints might want to look at alternative channels that would not involve the extent of duplication that their bringing in Denver or another channel might cause.

Senator EXON. Thank you for your answer. I wish you would take a look at it. I said that when I started out I hoped that we would not have to have legislation in this area. The answer to your last question indicates that we might have to have legislation, indeed, in my opinion, Mr. Chairman.

Thank you very much.

Senator GORE. Senator Burns.

Senator BURNS. Thank you very much.

Chairman Sikes, I want to welcome you back. I understand we share some common things, like some of the same dirt under the finger nails and things like that.

I want to commend you. You have demonstrated already quite a lot of leadership in the FCC just for the short time you have been here. We came about the same time and I guess it is all sort of baptism by fire. And here we jump into this legislation.

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[1] The articles were not reproducable. See Fremont Guiding Tribune, Nov. 2, 1989, and Scottsbluff Star Herald, Oct. 10 and 11, and Nov. 15, 1989.

I also want to, in going over your statement this morning, compliment you on your approach to this issue. The re-examination of effective competition standard is very important and appropriate at this time.

Third, I would suggest that Congress pursue the less-intrusive target efficient means of achieving our goals. We have looked at this issue ever since we have been here, and what route do we take?

Do we take the competitive route? Or do we go back to the old regulated routes? And I think it is kind of coming down on the side of competition.

The exclusivity thing is causing us to get quite a lot of mail, too. But coming out of the broadcast field, I can understand how some people might be concerned about that. It is a vital concern to those people who own those broadcast properties. And I understand that.

As you note in your testimony, you champion the video dial tone approach to the question of telco entry into video services. Could you elaborate on this position and maybe explain to me why both cable and telco should not operate out of the same rule book?

What I am getting at, it looks like the rule should apply to—the same rule should apply to everybody in the industry. If we continue to permit cable to provide both conduit and content, why should not the same regulatory approach apply to the telcos?

Mr. SIKES. Well, let me speak first to the video dial tone. Today, we pick up the phone, we get an audio dial tone. Traditionally, that has meant that we can call somebody across town, or across the United States, or internationally.

Increasingly today, the audio dial tone also provides, in some markets at least, so-called audio tech services, which might include messaging services, might include data bases, say, in conjunction with a library.

I know that my daughter registered and chose her curriculum for her sophomore year at college from Bethesda, Maryland, even though she goes to the University of Wisconsin. And she specifically used the touch-tone telephone to enter her decisions as to classes and times.

I see the development of a video dial tone. Where rather than just an audio dial tone, you get a picture on your monitor. Presumably, a menu that would tell you what you can get. And then, at the central office, the central telephone office, or conceivably a central office of a cable provider, you would have a switch that could engage in video switching.

So, that as you chose what you wanted, that switch would fulfill your desire, maybe for real-time viewing, maybe for down-loading for a compact disk for later viewing.

When I talk about a video dial tone, that is what I envision. I saw on Monday, referencing the Boston meeting of the National Association of Regulatory Utilities Commissioners, a GTE demonstration of video switching that was quite impressive.

And so, the technology that will facilitate this is really on the verge now and makes a whole enriched level of services quite possible.

I know Senator Gore has been quite interested in national fiber networks, and in the "smart network." Again, I think the developments are impressive in this area.

Turning to the rule book question, right now, in most states, cable cannot provide telephony. There are a few states, Illinois notably, where that is not true. So, as cable faces a legal block to getting into telephony, I think we have to be concerned about letting the telephone company being a fully vertical cable operator.

It also strikes me that legislative approach would be less likely successful, because of the concerns of various media that allowing that concentration of power through the local exchange, and through the extraordinary revenue streams of local telephone companies, might be just overwhelming.

Senator **Burns**. Going along with that line of what you just elaborated on as far as the Smart Networks and things. Will it be the priority policy goal of your commission to encourage more rapid deployment of fiber optics?

Mr. **Sikes**. Yes.

Senator **Burns**. Will allowing telephone companies to provide cable service, would that speed that along? Would that accelerate that development?

Mr. **Sikes**. I think there is a significant possibility that it would. The current copper wire network, particularly as the computer has enhanced its potential, can accomplish a great deal. But one of the things it cannot accomplish is the kind of video distribution that we are talking about.

As a consequence, when you block that sort of video distribution, you run a real risk of blocking commercial development. And this is something, if I can be indulged for about 30 seconds—overseas, they are looking increasingly at public investments to establish these kinds of networks. In this country, we have relied on the market to develop our communications infrastructure.

If we then get into the market and specifically set up barriers, it is less likely the market is going to develop the infrastructure and potentially the Government would then look at the challenge as it did, say, the interstate highway system, and believe that it has to get into the residential market to develop the infrastructure.

Senator **Burns**. Well, I just think the possibilities—you know, we that live in states where it is pretty sparsely populated, we have got to rely on a lot of these communications and the technology they afford.

And one of them, I think, goes hand in hand with something that concerns me very much, and I think it concerns your home state, too, and that is rural health: the ability with large medical centers to communicate both visually and by voice with some of our areas in rural health concerns.

So, I would offer the invitation. We might have some field hearings in Montana. I would sure like for you to think about that. We will go in the summertime, unless you ski.

Mr. **Sikes**. Good, excellent. Let me say, I look forward to that, returning as I will from Senator Stevens' state in mid-July, where we are going to salmon fish.

Senator **Burns**. I will join you on that trip.

But we want to issue that invitation to you. Because there is a lot of concerns out there in the country that we could sure talk about. And this one in particular, because we understand it is very important.

And I thank you, Mr. Chairman. Thank you very much.

Senator GORE. Senator Stevens.

Senator STEVENS. Thank you, Mr. Chairman.

I will not be long because that quorum call is for me. And I do hope that these hearings are not the hearings on the legislation that I have been reading. That these are just preliminary oversight hearings.

Senator GORE. You cannot ever tell.

Senator STEVENS. We better have 60 votes, then.

Senator GORE. Let me say that yesterday Senator Danforth stated that his intention, and I know it is shared by Chairman Inouye and Chairman Hollings, is to proceed very deliberately, and at some point next year have hearings in advance of acting on the legislation itself.

Senator STEVENS. I was not able to stay all day yesterday either. And I appreciate that clarification, because those of us who live out there in the remote tentacles of this communication system have to have time to examine the impacts of these changes.

Let me ask a couple of questions of you, Mr. Sikes. In the first place, I remember so distinctly the first time I went from here back west and had to go by railroad and through Chicago. And Chicago made you get off one train and go all the way across town and get on another one, you remember.

The problem that I have with these proposals, I see as more and more interference from the municipalities in creating fiefdoms that you have to pay dues in order to get through.

Have you examined these to see what kind of roadblocks are going to be placed in the way of the development of national cable as we have had national telephone and nationalize other concepts? Or has FCC taken a position on national cable?

Mr. SIKES. Well, first of all, in my testimony that I filed with the committee, I have outlined very specifically what I think are the extraordinarily positive developments from the Cable Act of 1984, although I have also been a bit critical of it because it tended to allow monopolization of franchises.

But, clearly, I think we need to think of this in a national cable sense. In response to an earlier question, I indicated that the municipal history in the area of cable has not been such that I would recommend a significant re-empowerment of municipalities in the cable area.

But some re-empowerment will undoubtedly result.

Senator STEVENS. I am pleased to hear that. And I do not want to prolong this, as I said. And I may have some other questions later for you and other witnesses.

But one of the things that bothers me is that Congress constantly imposes upon your agency additional responsibilities, additional duties. It looks like we are doing it again now. And yet, my memory is we constantly also reduce the amount of money you have available.

What is the situation with regard to staffing of the FCC now and the ability to keep up with these new demands?

Mr. **Sikes**. Well, I would say it is not overly attractive. There has been a substantial decrease, in real terms, in both staffing and resource availability generally. You know, we obviously are in difficult times. But what has happened in deregulation is mostly positive. But clearly it has expanded, not contracted, the responsibilities of the FCC.

When there was a monolithic telecommunications presence, for example, there were many fewer complaints than there are now that we have a very diverse telecommunications presence.

As we move toward opening up the local exchange network and opening up additional opportunities for the telephone companies, we need to make certain that discrimination and cross-subsidization do not occur. And those are very complicated matters.

So, generally, I think that our resources are not equal to a 21st century FCC.

Senator **Stevens**. I would like to study some kind of fee for service proposal and some additional fees for utilization of your quasi-judicial functions. It just seems to me that there has to be some accommodation to the needs of your Commission to be able to grow and acquire the expertise.

You must be having the same problem all the rest of government is that all the people that you train that are becoming experts suddenly are hired by the people that are appearing before your Commission, and you have got a fairly rapid turnover.

Is that right?

Mr. **Sikes**. Yes. Although, I would quickly add that one of the—I have only been there three months—but one of the things that has been a bit surprising and certainly reassuring is that we have a number of excellent senior-level people who regard highly work at the FCC.

I think, it is, again, one of the important institutions that people like to come and to work at.

Senator **Stevens**. Maybe we ought to ask someone to make a study and see what the pressures are on it. Because I have the opinion that you do have some very dedicated people who have stayed on despite the rather substantial offers from the outside of government.

But it does also seem—we are coming into a period now, what I like to call tumbling technology. You are going to have a group to be able to keep up with this technology. And I would hope that Congress does not get in the way of that tumbling technology.

I think the 1984 Act has worked. It has succeeded. It may mean, even as Mr. Malone said yesterday, that it is time for Congress to put some brakes to it. But I hope they are brakes that you have the right to pose, rather than us putting them on automatically.

And that in itself is going to increase your workload. I do believe that we need to take into account the extra burdens that are going to be on your commission. If we do what it seems that this commission—this committee is thinking about proposing.

And I would rather see it done in a discretionary fashion rather than a mandatory fashion, which as I said increases the burden. And I would like to request that you consider that some time over this recess. And give to some of us who would like to see a strong viable Commission some outline of what you think is your increased needs.

And I know that the OMB is going to tell you that they cannot give them to us—you cannot give those figures to us. But I can tell you, we can get them.

And I hope you are prepared next time you come to answer the questions about what you do need. I intend to ask you those questions of your first appearance here in January so that we can pursue it through the appropriations process and get you the type of assistance you need to deal with this issue that is coming up.

Thank you, Mr. Chairman.

Senator GORE. Thank you very much.

Point of clarification. Chairman Sikes, you referred to a report due at the end of the year. This is on the nature of competition in the industry and will cover satellite dish issues?

Mr. SIKES. This is, I am told, required under the Satellite Home Viewer Act of 1988. Specifically, it is an inquiry into possible unlawful discrimination by satellite carriers against distributors in the provision of super-station and network station programming for private home viewing by satellite dish owners.

Senator GORE. The report will be available to the committee before the end of the year?

Mr. SIKES. Yes. Specifically, it is required by statute as of December 31, 1989.

Senator GORE. Will it include the decoder issues?

Mr. SIKES. Well, there are two other open proceedings, one involving syndicated exclusivity, that relate to satellite distribution, and the other involving encryption.

I think those will be handled separately. I do not have a time that I can give you on that.

Senator GORE. Are you aware of what has happened with the decoder business?

Mr. SIKES. I am aware generally. Maybe not as specifically.

Senator GORE. Well, some of us have proposed for some time that there be an FCC standard for decoders so there can be some competition.

One company makes them now. They were successful in preventing along with the cable industry preventing passage of the satellite legislation. They said do not worry, we have got it taken care of, no problem. The private market will do this just fine, even though it is a monopoly.

Now they have stopped selling the decoders. They said it is fool-proof; well, it is not fool-proof. Now, the few that are available, the price is going way up. They said after volume production the price would go down. It has gotten much worse. The only way you can get one now is by buying a very expensive unit that has a lot of things that you may not want or need at all.

It is really a mess. And they are even—they even have the audacity to suggest that the consumers ought to foot the bill for replacing the current defective technology—easily broken, the code is easily broken—with a whole new device, where the consumers would have to pay twice. It really is an outrageous situation.

Let me ask one other question and then recognize Senator Danforth.

On the satellite television issue, some of us have proposed that if a programmer makes available programming to satellite dish owners and distributes the programming through cable companies, they ought not to be allowed to discriminate against retailers or distributors that are not cable television companies.

Do you understand the point?

Mr. SIKES. Yes.

Senator GORE. The cable television company as distributor to satellite dish owners has a structural conflict of interest. They have a built-in incentive to keep the price at or above the level paid by the cable customer for the same programming.

In the competition between movie theaters and videotape rental stores, since the distribution mechanisms for the product are completely different and the cost borne by the consumer is so much larger if the consumer patronizes a video tape rental store, we have seen the forces of supply and demand push the price for videotape rentals down to very low levels, $2 a night, some places even $1 a night.

If the people who own the movie theaters control the supply of programing and were able to dictate the prices, they might be tempted to keep the videotape rental prices up to or above the level charged for the ticket to get in the movie theater. They do not. There is competition.

The supply and demand lines cross at different points. And the price is lower where the customer bears the capital cost of purchasing the VCR and making two round trips to the videotape rental store, than where the movie theater operator bears the capital cost and the customer only makes one round trip.

In this situation, you have a very similar set of economics. The cable industry bears the capital cost of the distribution. And yet in the satellite dish industry the customer bears the capital cost of distribution.

One would naturally expect the price for watching the program to be lower where the customer is bearing the capital cost. But because of the artificial control over the source of programming the price to the satellite dish customer is kept at or usually above the price paid by the cable customer.

It is a market concentration issue. It is an unfair market leverage issue, and I hope that you will address it.

Now, the new technology we heard yesterday of KU band, is one satellite up there—has how many transponders? Fourteen transponders. The large multi-system operators are negotiating right now to purchase eight to 10, I believe, of those transponders.

Senator Danforth.

Senator DANFORTH. You need not answer that question.

I also am going to have a nonquestion. And then I have to go. I want to apologize for not being here. But it has been one of those days sort of typical of the last days of a session of the Congress. But I do have just two comments.

One is to say that really I cannot think of anybody in the government for whom I have a higher regard than I do for the chairman of the FCC. He is a person I have known for some years in a number of different capacities. And I think he is off to an outstanding start as the chairman of this Commission, particularly the actions that have been taken relating to indecent material over the radio. I think that that indicates both the strength of Chairman Sikes and the fact that when he says something, he does it.

This is what kind of thing he talked about when he appeared before this committee, Mr. Chairman, and he follows through. And I think it is very refreshing and very, very encouraging. And I want to commend you for this.

The other point that I want to make, and it just really is a statement rather than a question. But some people would say, well, with respect to the legislation that was introduced a couple of days ago on competitiveness in the cable business, well, let us let the FCC act; let us turn this over to the FCC. And regardless of my very high opinion of Al Sikes—he is, I do not know, the third, or fourth, or fifth chairman of the FCC, who has held that office since I have been here.

And it is not always the case that FCC chairman are particularly responsive to the views of the members of Congress. We did make an effort relating to must carry to get the attention of Mark Fowler. And it was the biggest wasted effort. I mean it was—as I said to him, you know, it was like spending a long time and having very good staff work, drafting a 15-page legal brief and having him sort of cut it in half and use the backs for scratch paper. It was just absolutely pointless.

So, I have to say Commissions change and chairman change—although, I hope this chairman will not change for a long time—but, I think that the matters that were raised by the cable bill that was introduced a couple of days ago are matter of fundamental policy.

And that is what Congress is in the business of doing. Congress should be in the business of establishing fundamental policy. For that reason, I believe, that legislation is in order. And I believe that this is something that cannot be left to the Commission.

Senator GORE. Thank you very much, Senator Danforth.

And I want to associate myself with your words of praise for Chairman Sikes. I expressed a similar sentiment at the beginning of his testimony. And I think that sentiment is shared, Chairman Sikes, by all the members of this subcommittee of whom I am aware.

And we want you to keep on taking this kind of dedicated approach to your work. And we are really delighted that you are here.

Senator Pressler.

Senator PRESSLER. I do have one question that I will ask. That is, the wireless cable people tell me that the FCC is still grossly understaffed to process applications, or there is a slowness there.

What are you going to do to help this technology get out to the people? You have said you are going to speed up the process. Are you increasing staff in this area? Or what will it take?

Mr. SIKES. I have asked for a report on that not next week but the week following. Whether we have to increase staff, improve procedures, or exactly what, I am not certain.

But the initial report I have gotten is that it is not a very heavily staffed area. So that characterization might be quite valid.

Senator **Pressler**. Mr. Chairman, I shall ask the rest of my questions for the record.

Senator **Gore**. Thank you, Senator Pressler.

And Chairman Sikes, thank you, very much for your appearance here today.

Mr. **Sikes**. Thank you, Senator.

Senator **Gore**. Let me invite to the witness table, Edward Fritts, president of the National Association of Broadcasters, and Preston Padden, president of the Association of Independent Television Stations, Inc.

If we could come back to order. If our guests could help us in that regard, we would appreciate it.

Our panel is made up of Eddie Fritts and Preston Padden. I have given your titles. And I want to welcome you officially and tell you that your full prepared statements will be put into the record in full. You are both well-known to this committee and considered as friends. We are delighted to have you here. And, Mr. Fritts, why don't you begin and proceed as you see fit?

STATEMENT OF EDWARD O. FRITTS, PRESIDENT AND CHIEF EXECUTIVE OFFICER, NATIONAL ASSOCIATION OF BROADCASTERS

Mr. **Fritts**. Thank you, Mr. Chairman. We appreciate the opportunity to testify here today. You have asked us here to discuss what has occurred since the Cable Act of 1984 went into effect. So, let me give you some brief highlights.

The cable industry has doubled in size to a $15 billion a year industry. The value of cable systems has increased from $600 per subscriber to $2,700 per subscriber. Said another way, that means that a system with 20,000 subscribers was valued at $12 million, and now that same system with no improvements and the same number of subscribers is valued at $54 million.

Cable is the monopoly gateway into over half of our Nation's homes. The cable operator has total control over what signals are available to those homes. Through unlimited horizontal concentration, 42 percent of the Nation's cable households are concentrated in the hands of four giant multiple system operators.

A recent GAO study found that rates to the consumer have climbed 29 percent in less than two years since deregulation took effect.

When the Cable Act was passed back in 1984 must carry was in place at the FCC. The cable industry challenged those rules in court, and today local stations have no assurance of carriage. What's more, many stations have been displaced from prime channel positions by cable networks which are largely owned by the vertically integrated MSOs.

Cable today stands as an unregulated monopoly. It is not regulated by the cities. It is not regulated by franchising authorities. It is not regulated by the Federal Communications Commission. It is not regulated by the Congress, and it is not regulated by competition. Cable, in fact, is the regulator of today's marketplace.

In short, in our opinion, the 1984 Cable Act has failed abysmally.

Cable's unrestricted monopoly operations, the use of compulsory license, its power to restrict access for local broadcasters and its use of a triple revenue stream of subscription rates, advertising and pay-per-view has led to a completely distorted marketplace. Sports siphoning is a prime example of how distorted this business has become.

Mr. Chairman, it seems to me that there are three options for this panel.

First, you can do nothing and the situation will continue.

Second, you can provide competition to cable perhaps by allowing the telephone companies into the cable business, but I think everyone agrees that will take 15 to 20 years and cost billions of dollars.

Third, you can look to reregulate cable in a sensible fashion such as restoring the balance to the marketplace and restoring sanity and reasonableness to the Nation's cable industry. We believe reregulation is the answer, and we further believe that S. 1880, the landmark legislation introduced and cosponsored by both of you Senators is the way to go.

S. 1880 provides for reasonable must carry and channel positioning rules, better regulation of effective competition, and it places limits on the growth and integration of the cable industry. In our opinion it represents a carefully thought out solution to the many problems which we face in the wake of the Cable Act of 1984.

In your letter of invitation, you asked us to briefly discuss the issue of telco entry which some believe is a better solution. As I mentioned earlier, our estimates are 15 to 20 years at best before the phone companies could provide any significant level of competition. And for rural consumers, it may never be economically feasible to provide service. If it is not feasible now for cable to wire the rural areas, it is unlikely to be feasible for the phone companies to wire those same areas in any expeditious timeframe.

Beyond that, if there is to be true competition, then we cannot allow the telephone companies to merely gobble up the cable companies. All that would do is replace one monopoly with another. Lifting the telco-cable cross ownership ban will not solve the problem. And under no circumstances should the giant telcos be allowed to provide content control of programming. Vertical integration has not worked for the consumers in the cable industry and it certainly won't with the telcos.

Now, in deciding to pursue telco entry, it is clear to us that the telcos have looked at the cable model. It is rate deregulated. It is horizontally and vertically integrated. And it is without any serious competition. No wonder the telcos lust after the cable business.

But, Mr. Chairman, that model is wrong. It is wrong for the telcos. It is wrong for cable. It is clearly wrong for the American people. It is based on faulty premises, and it does not serve the American consumers well. We need to change that cable model through responsible reregulation and not hand it over to another monopoly.

Any attempt to allow telco entry must be carefully crafted both legislatively and through regulation. And we see that process taking much too long to solve the problems that broadcasters and the American public have with this current situation.

I would urge the committee to use Senate Bill 1880, the Cable Television Consumer Protection Act, as its focus for resolving the problems posed by this Cable Act.

As always, Mr. Chairman, we appreciate this opportunity to appear before your panel.

And if I might take just one more second, I would like to acknowledge that today may well be the last day that my friend, Preston Padden, and I appear together. He is changing jobs at the end of the year. I just want to acknowledge for the record what a tremendous advocate he has been for independent television.

Thank you.

[The statement follows:]

STATEMENT OF EDWARD O. FRITTS, PRESIDENT & CEO, NATIONAL ASSOCIATION OF BROADCASTERS

Thank you, Mr. Chairman. I am Edward O. Fritts, President and Chief Executive Officer of the National Association of Broadcasters. NAB represents more than 970 local television stations, the major broadcasting networks, as well as more than 5100 radio stations.

NAB applauds you and the Communications Subcommittee for holding comprehensive oversight hearings on implementation of the Cable Communications Policy Act of 1984. These hearings are the latest in a series that have examined critical issues of importance to our industry, including media concentration, the state of competition within the video marketplace, and the importance of must carry and channel positioning protections for broadcasters and their viewers. These hearings have demonstrated that growing problems are presented by unregulated cable monopolies, which have been allowed to dominate other providers of video programming. NAB is pleased to have this opportunity to summarize its concerns about cable and the 1984 Act.

Only five years have passed since Congress enacted cable legislation to assist what was viewed as a struggling, nascent industry. Today, the communications world is radically different. It is becoming increasingly apparent that the goal of the 1984 Act was not accomplished -- to remove government regulation of cable and replace it with marketplace regulation of cable. Instead, cable itself has become the regulator of the marketplace.

PROBLEMS WITH THE 1984 CABLE ACT

Hindsight has illuminated a number of key flaws in the 1984 Act which have created these unintended consequences. As far as the broadcasting industry is concerned, the principal failure of the Act is that it did not codify rules that governed cable carriage of local broadcast signals. Congress drafted and passed the Act under an assumption that the FCC's must carry rules would stay in place. As this Subcommittee knows, these rules have been struck down on constitutional grounds, although the courts have made it clear that carriage rules per se are not unconstitutional.

At the same time, cable continues to enjoy its compulsory copyright license. This license permits cable to retransmit our local signals without our consent and without payment, even though a considerable portion of the basic fees cable receives from its subscribers is attributable to our signals. It is becoming increasingly apparent to television broadcasters that the current regulatory scheme forces our industry to provide a sizable subsidy to cable.

With its present unbridled discretion over carriage and the positioning of the stations it does carry, cable now has the ability to act as the gatekeeper to America's homes. Local television stations have no assurance that they can reach the communities they are licensed to serve. NAB believes that constitutionally-sound must carry and channel positioning legislation can be crafted, and that such provisions are needed to restore balance to the video marketplace.

Other problems with the Act are apparent. It allows local governments to issue monopoly franchises. As a result, almost no cable system faces direct competition in its own market. Only about 60 of the more than 8400 franchised cable systems across the country now face "overbuilds." In the absence of carriage protections, local stations and their viewers have no alternative but to deal as best they can with their local cable monopoly.

The Act failed to establish clear, reasoned standards for "effective competition." The FCC's inexplicable decision to use the presence of 3 or more television signals as its standard for effective competition to cable has resulted in virtually nationwide deregulation of basic cable rates. The impact on cable subscribers is well documented. For example, a General Accounting Office study showed that rates for the lowest-priced tier of basic cable service increased nearly 29%, from December 1986 to October 1988. Rates for basic and pay services combined increased about 14% during that time period. When broadcasters compete against cable for sports programming and other offerings, we face an industry that can raise the stakes with the knowledge that it readily can pass its higher costs directly through to its customers.

The Act failed to restrict the horizontal growth of cable. Ownership of cable is becoming increasingly concentrated in the hands of a few huge conglomerates. In 1985, about 29% of all subscribing households were served by the top 5 "MSOs." In 1988, that figure had grown to about 35%. After the Time-Warner merger, the top five MSOs now control 42% of nationwide subscribers, and the top ten MSOs control nearly 54% of the country's subscribers. Local broadcasters clearly are not competing against a struggling "Mom and Pop" industry.

The Act did not restrict vertical integration of cable, the interlocking ownership of cable systems and many of the programming services that are carried on those systems. That integration, and the growth of cable advertising, has created economic incentives for cable to favor its own programming interests over the offerings of television broadcasters and other video providers.

The Act also eliminated virtually all local regulatory control over cable. Consumers, of course, have virtually no recourse within their local governments when they have problems with cable. Broadcasters also have no ability to seek to have local communities mediate carriage concerns with cable.

In short, the 1984 Cable Act has awarded extraordinary and unfair advantages to cable. Broadcasters welcome competition, but it must be on fair terms. We cannot serve our local communities adequately when we are forced to go up against unregulated monopolies that have the ability to act as gatekeepers to the homes of America. The video marketplace simply cannot work under these circumstances.

LEGISLATION ON CABLE IS NEEDED

Corrective action is required. NAB urges Congress to pass legislation that will help to return fair competition, by re-regulating cable in several important areas. This week, Senator Danforth (R-MO) and 13 other members of the Senate introduced such legislation, the "Cable Consumer Protection Act of 1989" (S. 1880). NAB enthusiastically supports this bill. We believe that this legislation will help to return fair play and common sense to the video marketplace.

This legislation would condition cable's compulsory license with must carry and channel positioning obligations. NAB supports this approach. We believe that providing cable with such an option will help this legislation withstand the inevitable constitutional challenges in the courts.

The bill also includes a number of other important elements. It restores to local franchising authorities a measure of control over cable, including more ability to regulate cable services and facilities. It redefines "effective competition" to establish a standard which is based on the presence of other multichannel providers. It also addresses both the vertical and horizontal power of cable, by capping its growth at 15% of nationwide subscribers and by limiting cable's ability to discriminate against competing services with the programming in which cable has a financial interest.

All of these provisions will help restore a marketplace in which broadcasters, cable and other video providers can compete on more equal terms to serve American consumers. NAB realizes that many of these provisions are complex and controversial, and that the authors of the bill expect that it could be revised following these hearings as the legislative process unfolds. NAB will be pleased to continue to work with its authors and the Subcommittee in these efforts.

TELCO ENTRY INTO CABLE SERVICES

NAB believes that re-regulation of cable provides the most direct and immediate means of addressing competition in the video marketplace. We are aware, however, that a number of observers, including some members of Congress, favor additional steps. They also would seek to subject cable to additional competition from the telephone companies by repealing the telephone/cable cross-ownership provisions of the Cable Act. They believe that the telephone companies are the most likely industry to provide direct competition to cable. Some also seek to encourage the development and installation of newer transmission technologies, such as fiber optics, by opening up new business opportunities to the telcos.

NAB agrees that direct competition to cable in a market would address many of the carriage concerns that the must carry and channel positioning rules are designed to solve. We also recognize that as the technology offered by the telephone companies improves, they will be able to readily carry video signals in the future. The technological, economic and policy hurdles that must be crossed, however, before the telephone companies should be allowed to provide video services are very significant.

NAB and our membership is devoting increasing attention to the issues that surround telco entry into video services. We have formed a Task Force to examine these issues in more detail and to provide policy recommendations to our Board. Two basic guidelines already have emerged from our study of these issues, however. NAB is utilizing these guidelines to shape the positions that we will urge Congress and the federal government to follow as you consider policy changes.

First, NAB believes that if the telco/cable cross-ownership provisions of the Cable Act are amended, the telephone companies should not be permitted simply to purchase existing cable systems. To allow them to do so would merely replace one monopoly with another. We believe that if the telephone companies are permitted to own cable systems within their service area, they should be directed to provide the second video wire to the home, wherever possible. In other words, we support a pro-competition policy in which the telephone companies should be allowed to enter into cable service only as an "overbuild." Such a policy would create true competition between cable and the telcos, and would benefit both television stations seeking carriage and consumers seeking the best rates for cable service. This policy also would appear to provide incentives for both cable and the telephone companies to upgrade the wires that pass the homes of our nation.

Second, we believe that the telephone companies should continue to be restricted to their traditional role as carriers of content, not owners of the content they carry. If the telcos are permitted to offer cable or other video services, NAB urges that such restrictions be maintained on their ownership and control of content of those services.

Hard experience with cable has demonstrated how competition is stifled and broadcasters and consumers harmed when the owners of a multi-channel distribution plant are allowed to have vertical ties to the content carried over their systems. These dangers are magnified enormously when telephone companies are involved. Given the huge size of that industry, its regulated and unregulated revenue streams, and the difficulty in preventing cross-subsidization of competitive services with funds derived from regulated services, it is apparent to NAB that Congress and the FCC should continue to apply common carrier principles to the telephone companies if they are allowed to deliver video services.

NAB urges Congress to consider amendments to the existing telco/cable cross-ownership provisions only after careful deliberation of the enormous consequences of such legislation. The potential effects of these changes on competition in the video marketplace and our nation's system of free over-the-air broadcasting are enormous. NAB will be pleased to continue to take part in your deliberations on these issues.

On behalf of NAB, I appreciate this opportunity to testify. We will be happy to respond to any questions you may have.

Senator GORE. Well, thank you very much, Mr. Fritts.

You have sort of been introduced right there, Preston.

Mr. PADDEN. I guess I will have to pay him after the hearing.

Senator GORE. We wish you well too. You are going to one of the networks, the upstart networks, aren't you?

Mr. PADDEN. Yes, sir.

Senator GORE. Well, we wish you well. And we are delighted to hear your presentation today as President of the Association of Independent Television Stations, and we value your expertise. So, please proceed.

STATEMENT OF PRESTON R. PADDEN, PRESIDENT, ASSOCIATION OF INDEPENDENT TELEVISION STATIONS, INC.

Mr. PADDEN. Thank you very much, Mr. Chairman.

I think one of the most fundamental shortcomings of the Cable Act is its failure to come to grips with what cable really is. And I think as Congress approached the adoption of the act, there were two basic choices, and we have prepared a little chart to outline the alternatives we think Congress had.

It could have approached cable as a monopoly utility carrier, and if it had chosen that approach, cable would have been entitled to exclusive franchises, special copyright provisions, guaranteed use of utility easements, pole attachments. But cable would have been subject to separations requirements separating the conduit from the content, access requirements to ensure that people had access to this monopoly utility carrier and rate regulation.

Alternatively, the act could have approached cable as a competitive medium of expression in which case cable would have been entitled to full First Amendment rights, the right to integrate vertically into programming, to discriminate against others they weren't vertically integrated with, and would not have been subject to rate regulation.

But in this competitive model of development, cable would have been subject to full copyright, to competition from other wire line carriers. They would have had to negotiate for the right to dig up my front lawn rather than rely on utility easements. And they would have had to negotiate for pole attachments.

And I think it is obvious from this outline that what cable did was a great job of broken field running where they got the benefits of both models and the detriments of neither. And that in our judgment underlies the problems we have in the act today.

We think the most fundamental shortcoming of the act was the failure to establish a separation between the ownership of the conduit and the ownership of the content trying to get through there. And this was the recommendation of a cabinet committee on cable in 1974. Their number one recommendation was to separate the ownership of conduit and content. Unfortunately, that did not happen. The only vestige of that in the Cable Act is the leased access provision, and we will show you why that didn't work at all.

Failure to require this separation has led to this kind of vertical integration. That is a flow chart of TCI, poor, vulnerable John Malone up here with all of these program services he has been saddled with. And I don't think it takes a rocket scientist to figure out that these are the services that are going to get through the TCI systems in the most advantageous way.

Now, a couple of months ago, Mr. Mooney sat here and he proffered for your consideration a report from an economist named Klein that purported to say that there was no correlation between what companies like TCI owned and what got through their system. And I think it strained credulity at the time, but in yesterday's New York Times, John Malone was quoted as saying, "We invest for access." Now, if that is true, then the entire Klein report is discredited because the premise of the Klein report was that ownership of program services has nothing to do with what got carried and what people had access to.

I would also point you to the antitrust complaint that Viacom filed against Time, Inc. in which Viacom, itself a major cable MSO, said—and these are quotes from their complaint, a sworn complaint—that "each cable operator is a monopolist in its local market," that they "refused access" to non-vertically integrated services. Where they do provide access, they provide it on a discriminatory basis. And we think it is particularly important that Viacom, itself a cable operator, acknowledges that vertically integrated MSOs disadvantage other programmers, including local broadcasters with regard to channel position.

Now, I think the act's failure to separate conduit from content has led to this mess, and it is even worse than that. I want to show you a provision of section 612(d) of the act, and I think anybody that reads it who voted for the act is going to cringe when they realize how they got conned.

This is from the leased access provision, and that was the provision that was supposed to open up the cable conduit and ensure fair access for non-vertically integrated programmers. And it says that in any court action to consider the reasonableness of the cable operator's leased access terms, the court shall not consider the price, term and condition established between the operator and his own affiliated or owned services. It is exactly backwards, Mr. Chairman.

In the telephone model, there is an enormous amount of effort made to make sure that interconnection is provided to other parties on exactly the same terms or no less desirable terms than provided to their own affiliate. And here when the Cable Act was getting passed, somehow somebody snuck in there and dropped this line in there so that they could favor their affiliated program services, and they would not have to deal fairly with non-vertically integrated services.

Now, let me add that I think a lot of the blame for the mess we have does not lie in the act, but in events taken by the cable industry itself since the act. They compromised to gain passage of the act, and they have now set about to bring lawsuits under the First Amendment to get rid of all the portions of the act they didn't like. They have sued to overturn the franchise renewal section, the public access section, the universal service section, the franchise fees. Even franchise fees they say violate their First Amendment rights. And, of course, the cable industry has twice gone to court to get rid of the must carry rules.

And somebody asked at yesterday's hearing if the cable industry says they want must carry, and the broadcasters say they want must carry, and the Congress wants must carry, why don't we have must carry. And the answer is that when the cable industry says they want must carry, they are not talking about the same thing that I think the Congress is talking about and we are talking about.

They come to us with proposals that would result in the must carry signals not being viewable on many sets hooked to the cable. Now, to me if must carry means anything, it means that when a consumer turns on a TV hooked to the cable, he is going to be able to see the local broadcast stations. But they keep bringing us proposals they call must carry where you wouldn't be able to see many of our members' signals.

And they also bring us proposals that would give them the right under the guise of on-channel positioning to shift us out of the good channels so they could pack them full of their own product. And they argue that we have no right to those channels in perpetuity. And I would just point out that S. 1880, just like Senator DeConcini's bill and just like Senator Lieberman's bill, would guarantee local broadcasters a chance to remain in the channels where they have been only so long as their cable operator had the right under the Compulsory Copyright Act to use our signals for free. So, it is not a matter of being in perpetuity unless this copyright subsidy continues in perpetuity.

And somebody else asked yesterday what the percentage of viewing to over-the-air broadcasting cable homes was. I don't think you got a complete answer. The answer is 72 percent of all viewing in cable homes is to over-the-air broadcast services for which the cable operator in the case of local signals doesn't pay a red cent. It is a tremendous subsidy to the cable industry.

And all we are asking in return is that they not jerk our channel position around, and yet they are busting our chops over this provision and saying that we are holding up a deal over it. Somebody said to me yesterday it is like the phone company gives you a phone number, you establish a business, get it going, and then the phone company decides that looks like a good number, and they take it back for themselves.

It is a situation we cannot tolerate, and I hope that the example from the 1984 act is clear to everyone. They are trying to trick the Congress and injure us just like they did many others in 1984. And we are simply not going to make a deal with them until we get a fair shake.

Finally, Mr. Chairman, I wanted to mention the issue of sports siphoning. I know Mr. Malone testified he is just a poor, vulnerable guy that can't do anything about the sports siphoning.

This is a reprint of an ad from a Nashville newspaper from Viacom Cablevision for pay-per-view of the University of Tennessee football games. You may not be able to see down at the bottom. It costs the consumer 20 bucks a game if he orders it in advance, 25 bucks if he waits until the day of the game. Last year Southeast Conference football games were available free of charge on local independent stations throughout the southeast. This year the cable

MSOs that own Turner Broadcasting pulled the plug on those free broadcasts, and this is what you get instead.

Now, last week a company that Mr. Malone owns a big piece of called Prime Ticket put out a report that purported to show there was no siphoning of sports off of free TV. I got a copy of it faxed to me when I was in Los Angeles last week. I was driving down Pico Boulevard, and I looked up and here was a billboard from Mr. Malone's company, Prime Ticket. And you can see the copy says: "No cable, no Gretzky. No cable, no Magic." And that's the message they are giving to consumers. And I would assert it is considerably different than the message you heard yesterday.

That concludes my testimony. Thank you very much, Mr. Chairman.

[The statement follows:]

STATEMENT OF PRESTON R. PADDEN, PRESIDENT, ASSOCIATION OF INDEPENDENT TELEVISION STATIONS, INC.

Introduction

Thank you Mr. Chairman. My name is Preston Padden and I am President of the Association of Independent Television Stations, Inc., commonly known as INTV. America's 300 Independent television stations constitute the only commercial source of non-network television information and entertainment that is available free-of-charge to all consumers -- rich and poor, rural and urban, cabled and non-cabled.

When given a fair opportunity to compete, Independent stations have proven enormously popular with viewers. In May 1989, Independent stations accounted for approximately 25% of all viewing to advertiser supported television. However, our stations continue to struggle financially. According to the National Association of Broadcasters, in 1988 the average network affiliate station had a pre-tax profit of $3.9 million. By contrast, the average Independent station suffered a loss of $406,254.

We appreciate this opportunity to offer our views regarding the Cable Policy Act of 1984. At the outset, I would note that INTV supports, enthusiastically, the Cable Television Consumer Protection Act of 1989, which Senator Danforth introduced earlier this week along with thirteen original co-sponsors, including five members of this subcommittee. The bulk of my testimony will necessarily dwell upon problems in the structure of the Act as it affects the cable industry. However, Congress's purposes and objectives in adopting the 1984 Act were sound. Much of what you accomplished was good and has succeeded in expanding television viewing options for consumers. We do not appear here today for the purpose of convincing you to put cable back in the box, but to urge you to preserve the positive aspects of the Act while making those adjustments necessary to assure attainment of the goals and objectives established by the Congress. It is often said that we should not dwell on fixing what "ain't broke." Therefore, let me focus on some adjustments we consider critical to your task of assuring the best and most responsive television service to all the people of this country.

II.

Subsequent Events Have Conspired to Undermine The Goals and Objectives of The Cable Act

A large portion of the "blame" for the anti-competitive conditions extant in today's cable marketplace can be attributed to events that have transpired subsequent to the adoption of the Act. These events include the following:

- Unexpectedly heavy growth in cable penetration.

- Furious horizontal concentration of cable ownership.

- Cable's massive vertical integration into programming services.[1]

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[1] Appended as Attachment No. 1 are charts depicting the vertical integration of TCI and Time/Warner.

- Repeal of administrative "traffic rules" (such as "must-carry") regarding cable system operation.

- A relentless and surprisingly successful campaign of First Amendment litigation by the cable industry.

These events have undermined the purposes and objectives that Congress established for the Cable Act. For example, cable advocates have attacked the franchise renewal provisions of the Act arguing for a perpetual First Amendment right to operate their system. Group W Cable Inc. v. Santa Cruz, 669 F. Supp. 954, 975-76 (N.D. Cal. 1987). See also 679 F. Supp. 977, 978 (N.D. Cal. 1988). Cable advocates also have successfully attacked the public access and universal service requirements of the Act, arguing that these provisions violate the cable operator's First Amendment right to "speak". Century Federal, Inc. v. Palo Alto, No. C-85-2168 (N.D. Cal., September 1, 1987).

Similarly, cable advocates have attacked the franchise fee provision in Section 622 of the Act arguing that even a franchise fee violates the operator's First Amendment rights. See Century Federal, Inc. v. Palo Alto, supra; Erie Telecommunications, Inc. v. City of Erie, 659 F. Supp. 580 (W.D. Pa. 1987) aff'd on other grounds, 853 F. 2d 1084 (3rd Cir. 1988). Finally, of course, cable operators have succeeded in using First Amendment litigation to twice strike down the FCC's "traffic rules" relative to the carriage of local broadcast stations. Quincy Cable TV, Inc. v. FCC, 768 F. 2d 1434 (D.C.

Cir. 1985), cert. denied, 106 S.Ct. 2889 (1986); Century Communications Corp. v. FCC, 835 F. 2d 292 (D.C. Cir. 1987). Although the must-carry "traffic rules" were not specifically set forth in the Cable Act, their continued existence was certainly a fundamental premise of the Act. H.R. Rep. No. 98-934, 98 Cong., 2d Sess. at 70.

Thus, while the balance of this testimony will deal with the need for amendments to update the Act, a great many of the problems we face today are new problems which call for new legislative responses. They are the product of events that transpired subsequent to the adoption of the Act including, in particular, actions initiated by the cable industry itself.

III.

The Act Has Failed to Promote Competition In Cable and Has Left Cable in a Position to Stifle Diversity of Information Sources and Services

Two of the principle purposes set forth in Section 601 of the Cable Act are (1) to "promote competition in cable communications" and (2), to "provide the widest possible diversity of information sources and services to the public" (emphasis supplied). The Act has been notably unsuccessful in the attainment of these goals.

Simply stated, there is no competition in cable. Approximately 99.006% of all cable subscribers have access to exactly one cable system. In testimony preceding adoption of the Act, the then-President of the National Cable Television Association represented to the Congress that,

> "A consumer will have a couple of choices of cable companies. There will be two cable wires running down the street."2/

With the benefit of hindsight, it is clear that Mr. Wheeler's expectations were wildly optimistic.

The United States Department of Justice views cable as a "natural monopoly" and thus permits cable operators to engage in conduct that would otherwise violate the nation's anti-trust laws. Manishin, "Antitrust Regulation in Cable Television: Federal Policy at War with Itself", Cardozo Arts & Entertainment Law Journal, 75 (1987). In Federal Court litigation, cable industry "insiders" Turner Broadcasting Company and Viacom Inc., have described cable as a "monopoly". For whatever reasons, it is abundantly clear that the Cable Act's goal of promoting competition in cable communications has failed, and failed massively.

The Cable Act has also failed to reach its goal of providing the widest possible diversity of information sources and services to the public. Objective evidence demonstrates conclusively that the cable marketplace is not yielding program decisions

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2/ Thomas Wheeler, President of the National Cable Television Association at hearings before the Subcommittee on Communications of the Committee on Commerce, Science & Transportation, United States Senate, 98th Congress, First Session (February 16-17, 1983), pgs 126-127.

responsive to consumer preferences as the following examples illustrate:

- NBC was not permitted to provide consumers with an alternative source of general news in competition with CNN because of opposition from cable MSO's who subsequently secured equity positions in Turner Broadcasting System, owner of CNN.
- In order to gain cable access for its Consumer News and Business Channel, NBC was forced to sign written commitments not to provide the American public with a second source of general news in competition with CNN by converting CNBC into a hard-news service.
- Local broadcast stations have been dropped from cable systems and replaced with less popular program services in which the cable operator has an equity interest and/or sells advertising.
- Local broadcast stations have been shifted out of long-held channel positions and replaced with less popular program services in which the cable operator has an equity interest and/or sells advertising.
- In New York, cable consumers were forced to seek redress under the anti-trust laws in order to gain access to premium entertainment services other than those owned by their local cable system operator.
- Viacom, itself a major cable MSO, has filed an anti-trust suit against Time Inc. alleging anti-competitive actions regarding cable access and cable channel positioning.
- Major sporting events are being siphoned from free TV to cable; thus reducing, rather than expanding, the diversity of program choices for non-cable viewers.

IV.

The Act Suffers From a Schizophrenic View of Cable

Cable has long played the courtroom chameleon -- alternately posing either as a passive little antenna or as a dashing electronic publisher depending upon its strategic objective of the moment. In its lobbying for passage of the Cable Act, the cable industry put on a dazzling display of broken field running between alternative models for development of the cable medium.

Congress could have approached cable as a passive common carrier utility for the transmission of video to consumers. Alternatively, Congress could have approached cable as a competitive medium of expression. Each characterization carries with it its own set of benefits and burdens for the industry. In securing passage of the Act, cable managed to obtain most of the benefits of each of these characterizations, while suffering the burdens of neither.

As a passive common carrier utility, cable would be in a position to assert a right to exclusive franchises, special copyright arrangements, statutorily guaranteed use of utility easements and pole attachment regulations (the "must-carry" that cable likes). However, as a passive common carrier utility, cable would have to accept a clear separation between control of conduit and control of content, as well as access requirements and rate regulation.

Alternatively, in the competitive model, cable would be entitled to full First Amendment rights of self-expression, the right to discriminate against other speakers, and the right to vertically integrate and favor its own product. However, in the competitive mode, cable would be subject to full copyright liability, to competition from other wireline carriers, and to marketplace negotiations for the right to use real property easements and pole attachments.

The Cable Act never really comes to grip with an explicit characterization of the cable medium. Instead, cable managed to "bob and weave", thus securing the best of both worlds -- and the burdens of neither. The Act grants cable operators the exclusive franchises and access to utility easements and pole attachments appropriate for a common carrier utility, but without common carrier regulations, separations policy, access requirements or rate regulation. At the same time the Act grants cable operators the right to discriminate, to vertically integrate, and to favor their own product without the obligation to face competition or engage in marketplace negotiations for program product, real property easements or pole attachments.

This schizophrenia in the Act -- the failure to come to grips with the fundamental nature of the cable medium -- is the root of many of the problems evident in today's marketplace. Nowhere is this schizophrenia more starkly apparent than in Section 621 of the Act which simultaneously grants cable operators the right to use utility easements and at the same time prohibits utility-type or common carrier regulation of cable.

It is simply wrong to grant a single operator an exclusive franchise (whether de facto or de jure), which is a Federal statutory right to dig up private property for its own commercial benefit -- to install pedestals with signs proclaiming "Before you dig, call Miss Utility" -- and then permit the same company to exercise First Amendment rights to exclude others from its system, to shift the flow of traffic to benefit its own vertically integrated services and, in the final analysis, to decide what television consumers will -- and won't -- get to see.

V.

Failure To Include a Clear "Separations Policy" Was the Single Most Egregious Mistake In the Cable Act

The Cable Act's schizophrenic approach and events subsequent to the adoption of the Act, are coalescing as a major roadblock to the attainment of competition and diversity. Broadcasters, consumers and non-vertically integrated programmers now face the deadly triple-play of (1) a monopoly conduit, (2) that is vertically integrated, (3) but subject to no "traffic rules."

Nowhere is this problem depicted more starkly than on the Time/Warner cable system in Rochester, New York. Time/Warner produces programs. Time/Warner controls the only cable television conduit to more than 160,000 households in the Rochester market. Time/Warner sells advertising on 18 different channels on its cable system. Time/Warner has created a new cable "Independent station" (and even given it the broadcast call letters of WGRC) and awarded it a favorable slot on channel 5 on its system. Time/Warner -- as represented by NCTA -- wants the right to shift the local UHF Independent station from its current cable channel position on number 7, to a less desirable high channel position of 31.

According to a federal court complaint filed by Viacom, itself a major cable operator, Time/Warner uses its control of monopoly essential facilities to discriminate against other programmers regarding access and channel position on cable systems. Certainly, the experience of Independent Stations confirms the allegations of the Viacom complaint.

The danger of conditions such as now exist in Rochester (and in many other cable communities) was clearly foreseen prior to the adoption of the 1984 Act. For example, a 1974 Cable Report To The President by a Cabinet Committee on Cable Communications foresaw, with startling prescience, precisely the problems we face today. The Cabinet Committee (comprised of Elliott Richardson, Leonard Garment, Herb Klein, Peter Peterson, George Romney and Clay Whitehead) expressed its competitive concerns in the following terms:

> "Cable's multi-channel technology, together with the economic imperatives of a medium that is a natural monopoly, could lead to an even greater concentration of power than exists in broadcast television. When a single cable operator has the power to control the programming and information

> content of all the channels on his system, his monopoly power over the cable medium of expression is nearly absolute."

The solution suggested by the Cabinet Committee was a so-called "Separation Policy" described as follows:

> "We recommend adoption of a policy that would separate the ownership and control of cable distribution facilities, or the means of communications, from the ownership and control of the programming or other information services carried on the cable channels."

Two years later, the concept of a separations policy received the emphatic endorsement of a staff report prepared for the use of the Subcommittee on Communications of the House Committee on Interstate and Foreign Commerce. That report stated as follows:

> "We concur fully with the Cabinet Committee Report that it is of the utmost importance to implement the separations policy as soon as it is feasible to do so. The sound approach is to establish a market structure for cable that in itself serves the public interest, (i.e., the cable operator wants to lease channels or sell time on channels because that is his only business) - and not to permit an industry structure that invites abuse and then close government regulation to deal with the abuse." Cable Television: Promise Versus Regulatory Performance, 94th Cong. 2d Sess. at 90.

Precisely anticipating the anti-competitive practices now extant throughout the cable industry, the House Subcommittee staff quoted with emphatic approval the following excerpt from the Cabinet Committee Report:

> "Simply requiring the system operator to treat all channel users on a non-discriminatory basis without prohibiting him from having an economic interest in a user would not be adequate to prevent anti-competitive behavior. The cable operator could, for example, charge artificially high, but still non-discriminatory rates to users of his channels and use the excess profits from his system ownership activities to subsidize his programming affiliate. This cross-subsidization would place the other channel users at a severe competitive disadvantage." Ibid.

Failure to implement a clear separations policy is the single most egregious mistake now evident in the construction of the 1984 Cable Act.

NCTA recently commissioned a survey purporting to prove that cable operators did not favor their own vertically integrated services. However, daily events in the cable industry flatly contradict such arguments. For example, Viacom recently sold 50% if its Showtime Networks, Inc. (Showtime and The Movie Channel) to TCI. Last week's Multichannel News (November 6, 1989 at p. 1), reported that Home Box Office has offered equity deals to major MSO's "to secure wide carriage" of The Comedy Channel. Either NCTA's study is flawed and operators do favor their vertically integrated product or, savvy programmers like Viacom and HBO are needlessly parting with a lot of valuable equity. Indeed, earlier this month, a major international investment banking concern issued a "buy recommendation" for TCI stock, explaining that "Positive factors include TCI's ability to command equity interests in various facets of the home entertainment and communications business..." and that "...TCI is an attractive stock because it dominates a "monopoly" business that is still growing." (County NatWest USA, November 8, 1989).

VI.

The Leased Access Provision Has Not Worked

The only faint vestige of a separations policy evident in the 1984 Cable Act is the so-called leased access provision set forth in Section 612. Unfortunately, this section of the Act has proven to be absolutely useless in seeking to advance the objectives of assuring consumers access to the widest possible variety of video sources and services.

In the real world of today's cable environment, cable operators charge consumers constantly escalating, unregulated rates for basic service. A portion of the resulting revenue stream is then diverted in the form of "subscriber fees" that are paid to the cable operator's vertically integrated program services. This is precisely the kind of "cross-subsidization" envisioned -- and condemned -- by the White House Cabinet Committee and the House Communication Subcommittee staff.

Under the current system, the cable operator's vertically integrated program services are nourished with cash from the system operation. Any non-vertically integrated would-be competitor, seeking access through the leased access provision, would be forced to pay access fees to the system operator. Plainly, a program service paying for access would be at an insurmountable disadvantage as compared to those program services being paid subscriber fees by the system operator.

With the benefit of hindsight, it is apparent that the likely failure of the leased access provision was evident in the text of the Act itself. Section 612(d) explicitly provides that in any action brought challenging the price, terms or conditions for leased access "the court shall not consider any price, term, or condition established between an operator and an affiliate for comparable services." This most unfortunate provision is equivalent to providing that when evaluating the reasonableness of Local Exchange Carrier's interconnection with other carriers, the price, terms and conditions of the LECs relationship with its own affiliates should not be considered. Reductio ad absurdam! This provision totally gutted the efficacy of the leased access section, killing any hope of its acting as a curb against anti-competitive activities by vertically integrated operators.

To make matters even worse, in a colloquy on the House floor during passage of the Act, then Congressman Wirth stated, "The fact that the cable operator may pay for programming made available over channels other than leased access channels has no relevance to the arrangements that may be established for the use of channel capacity designated pursuant to this [leased access] section." Congressional Record, Vol. 130 No. 127 at H10441, October 1, 1984. In other words, the monopoly system operator is free to nourish his own channels while bleeding his competitors dry.

For irrefutable evidence of the failure of the leased access provision, one need look no further than the marketplace. Despite widespread instances of dropping of local broadcast stations and refusals to carry competitive program services, there is no evidence that excluded programmers have been successful in gaining access through Section 612. If the leased access provision was efficacious, Viacom would not have been forced to resort to litigation under the anti-trust laws in order to gain access for its services on Time/Warner cable systems. If Section 612 worked, NBC would be in the cable news business today and would not have paid an estimated $20 million in "tribute" to TCI to gain access to TCI's systems for CNBC.

VII.

Amendments Are Required to the Cable Act

For all of the reasons outlined above, Congress should move forward expeditiously to amend the Cable Act.

Traffic Rules

Congress should immediately enact "traffic rules" to govern the flow of video information and entertainment services over monopoly cable systems. Rules assuring the carriage of local broadcast stations and grandfathering their pre-Quincy channel positions are a must. The so-called "on-channel" positioning policy favored by NCTA is really just a clever PR ploy. It would enable operators to shift all UHF Independent stations out of the desirable low channels.

Effective Competition

Because it is plainly evident that there is no effective competition to cable today, the effective competition section of the Act should be amended. Cable systems should be deemed subject to effective competition only when they face a direct head-to-head multichannel competitor with substantial penetration in the marketplace.

Fair Compensation

As noted above, cable operators currently pay subscriber fees to their own vertically integrated services, but do not pay such fees to local broadcasters or to non-vertically integrated programmers seeking access under Section 612.

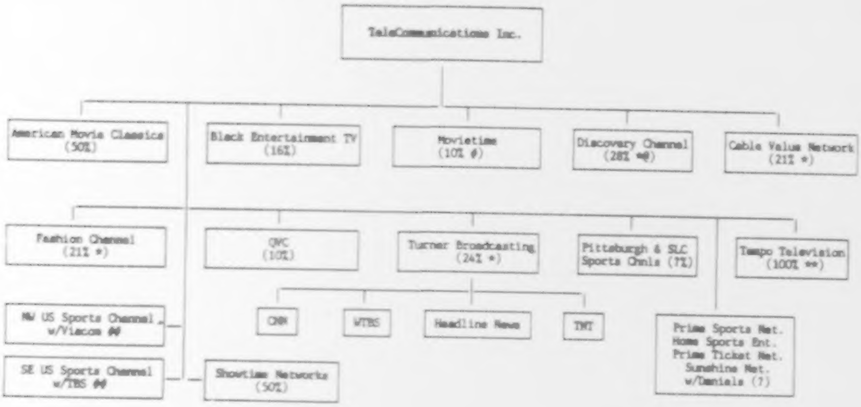
Congress should repeal the provision in Section 612(d) which prohibits consideration of the price, terms and conditions of an operator's relationship with affiliated program services. In fact, as in the telephone model, it is precisely the operator's arrangements with his own affiliated program services that should be the model for the terms of access for non-vertically integrated programmers.

Eventual Competition or Common Carrier Treatment

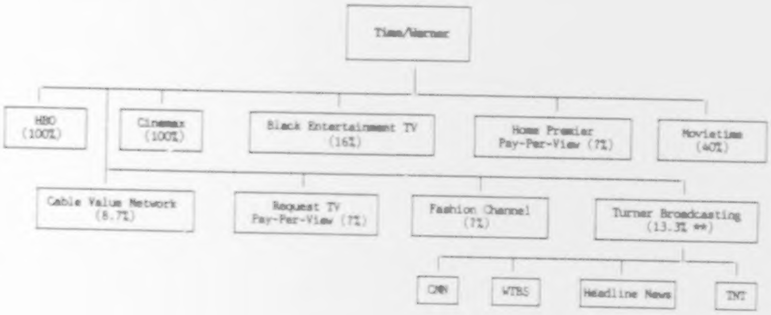
Longer term, the solution to the anti-competitive conditions now so evident in the cable marketplace, is to move toward the introduction of either (1) truly effective competition or (2) the institution of common carrier monopoly regulation. If the Congress turns toward telephone carriers for the introduction of competition, their entry must be strictly as carriers, without any vertical integration into programming. If our experience with cable to date has proved anything, it is the error of permitting common ownership of both conduit and content.

Telephone companies argue that they should be permitted to be programmers so that they can "prime the pump" of their new distribution systems. They repeatedly raise the specter of building transmission systems which may then lie fallow for lack of traffic. These arguments are ridiculous. Given the pent-up frustration with the cable bottleneck within both the broadcast and program production industries, it is inconceivable that telco fiber networks would have difficulty attracting traffic.

Attachment No. 1.--Vertical integration charts


TeleCommunications Inc.
American Movie Classics (50%)
Black Entertainment TV (16%)
Movietime (10% #)
Discovery Channel (28% *@)
Cable Value Network (21% *)
Fashion Channel (21% *)
QVC (10%)
Turner Broadcasting (24% *)
Pittsburgh & SLC Sports Chnls (?%)
Tempo Television (100% **)
NW US Sports Channel w/Viacom ##
SE US Sports Channel w/TBS ##
CNN
WTBS
Headline News
TNT
Showtime Networks (50%)
Prime Sports Net.
Home Sports Ent.
Prime Ticket Net.
Sunshine Net.
w/Daniels (?)

* Holdings include those of UA, United and other MSO's controlled by TCI.
@ TCI, Cox and Newhouse Cable recently offered to purchase the 40% of Discovery stock not already held by cable MSO's. Offer expires at the end of March 1989.
# Movietime ownership by United Cable which is controlled by TCI.
** TCI is leasing Temp TV to NBC.
## Proposed.


Time/Warner
HBO (100%)
Cinemax (100%)
Black Entertainment TV (16%)
Home Premier Pay-Per-View (?%)
Movietime (40%)
Cable Value Network (8.7%)
Request TV Pay-Per-View (?%)
Fashion Channel (?%)
Turner Broadcasting (13.3% **)
CNN
WTBS
Headline News
TNT

** Time Inc. has right of first refusal to buy controlling interest in CNN when Ted Turner sells his majority interest in the company.

Senator **Gore**. It is just hard to believe that there would be an inconsistency.

"No cable, no Gretzky. No cable, no Magic." In other words, if you don't pay per view, then you can't see them at all.

Mr. **Padden**. Well, in this case it is not pay-per-view. It is what they call pay cable and we call pay and pay again cable. But clearly the message is that you have to have cable to enjoy the local sports franchises in Los Angeles.

Senator **Gore**. Well, that is serious. It is not as serious as the Tennessee football game example.

But it is serious nonetheless.

Well, thank you both for your testimony here.

Let me ask you to continue for just a moment, Mr. Padden. In the earlier hearings, we had some discussion of a situation on Long Island where a small independent television station was advised that it would have to drop its news service before the area cable company, in this case Cablevision, would agree to carry that station's signal on the cable.

One of the witnesses in the earlier hearing felt that that was a complicated situation and that I hadn't stated it completely clearly.

I wonder if you have knowledge of that situation, and could you fill in some of the blanks as to what happened there?

Mr. **Padden**. I do not have detailed knowledge of that situation. What I know is this. There is only one commercial television station on all of Long Island, and it is WLIG out in Riverhead. And one company, Cable Vision Systems, owns the overwhelming majority of all the cable systems on Long Island. And the station's transmitter is out on the eastern tip of the Island. And Cable Vision carries them on some of the far out systems in Suffolk County, but has thus far, it is my understanding, refused to carry them on the large systems in Nassau County. The station has to be out there for technical allocation rules. But it is the only commercial TV station on Long Island.

And when you look at the situation and say here's the dominant cable system on Long Island and they are refusing to carry the only TV station on Long Island, the only answer that you can possibly reach is they don't want the competition for local Long Island television advertising.

Senator **Gore**. All right, very good.

Mr. Fritts, you share some of the same views I have expressed on cable television. However, you clearly and vigorously opposed telephone company entry at this time.

What if telco entry were predicated on a requirement that telcos would carry all local broadcast signals, network affiliate, independent, public, educational, all signals, within some geographically determined limits, and if channel positioning rules were enacted and if local broadcasters were allowed to negotiate for payment to carry their signals, would that change your view?

Mr. **Fritts**. Well, I think in terms of the telephone companies being involved in the broadcast business, we feel that they should provide a competitive conduit to the cable systems. We expressed to you that we think the cable model is wrong as it is currently construed, and that the telcos are looking at the cable model as the only premise for entering this business. And we think that is fundamentally flawed. Clearly I can see why they would want to come in on the same basis.

We are very concerned that replacing one monopoly with a larger monopoly with the dangers of cross subsidies, which are already clearly evident in the cable industry, would not be in the best interest of broadcasting or, for that matter, the American public.

Senator GORE. Now, yesterday Mr. Mooney claimed that broadcasters keep upping the ante on a must carry compromise. Is that a correct assessment in your view?

Mr. FRITTS. Well, I once was quoted as saying Jim Mooney would accept a must carry deal if it was his deal, and I think I still stand by that.

Mr. PADDEN. I would like to respond to that. I think there is some truth to that, and the reason is we reach what we think is a deal with them. And we turn around and we find that they have started to commit some new, heinous offense upon us that we hadn't anticipated.

And so, it is true that the next time we come back I think we quite responsibly seek to cover that base as well. It is like one of those games at the amusement park. Every time you try and hit the thing, it pops up somewhere else. So, I have some sympathy with the situation he faces, but it is because his members keep thinking of new crummy things to do to us out there in the field.

Mr. FRITTS. Mr. Chairman, I might also say that in that light, we have had difficulties with new problems which have emerged from the cable industry. I would also observe that over a year ago, both John Malone and Jim Mooney testified that in fact must carry was not a problem to them, that in fact there probably should be some accommodation on channel positioning and let's get on with the issue. Here we are well over a year later, and they have yet to come to terms.

Senator GORE. Senator Pressler?

Senator PRESSLER. Thank you, Mr. Chairman.

Mr. Fritts, yesterday's cable witnesses accused broadcasters of wanting not only must carry but also pay carry. Is that your position, or would it be fair to require carriage and payment?

Mr. FRITTS. There is an evolving debate taking place in the broadcast community. As Senator Gore pointed out, the cable networks are being paid by the cable systems X cents per month per subscriber. Seventy-two percent of the viewing in cable households, which basically drives the cable, is of over-the-air television. There seems to be an equity argument that could be made that if the cable industry is willing to pay for the cable network program services, by virtue of their advantage of the compulsory license, then perhaps they ought to look at paying the broadcast services as well.

So quite frankly, that debate is just beginning within our industry, and I am surprised at how much momentum it has picked up in such a short period of time. We do feel, however, that that debate is not mutually exclusive with must carry.

Senator PRESSLER. Now, yesterday the gentleman from Denver said that if we passed certain legislation, the cable companies would become mere collection agencies and would not have sufficient power to negotiate with program suppliers. Do you see a situation under which they could become mere collection agencies?

Mr. FRITTS. I find it hard to comprehend that they could be rendered to that position by Congress or by the FCC or by a combination of the two. And quite frankly I don't think that is the intent of the legislation that is being proposed today.

Senator PRESSLER. That was a term used yesterday to say what would happen. I was wondering what your response was.

Let me ask you this. Will the coming of the wireless provide competition in many areas for cable?

Mr. FRITTS. I think there might be some competition afforded in certain areas, but I must point out that it will be difficult to reach the entire country with any degree of penetration through the wireless cable to really make it effective in all areas. I am sure that there will be some areas that could be somewhat competitive.

Senator PRESSLER. Cable rates have gone up as much as 59 percent in a lot of communities. Why would you say that is?

Mr. FRITTS. Well, it's very simple. The Cable Act of 1984 deregulated cable rates and allowed cable to pass through their charges to the consumer. I think they have done that.

Senator PRESSLER. Have they abused the system?

Mr. FRITTS. Well, I think each Member of Congress can pull the figures from his individual state. I heard some figures that Senator Exon reported earlier, and they were much higher than figures that I had heard. So, I suppose in some areas they are balanced, in other areas they are abusive.

Senator PRESSLER. If you had to pick two or three areas where cable has, let's say, broken its promises it made during the hearings of 1982 and 1983, what would be the principal areas?

Mr. FRITTS. I don't know if this comes under the area of breaking a promise, but it seems to me that cable argued that must carry should not be addressed during the debate because it was embedded at the FCC. And as soon as the law was passed, they in fact continued to go to court to rid themselves of the must carry obligations.

Channel positioning, as Preston mentioned earlier and I have as well, has been an area where we think that they have, if not broken a contract, certainly broken good faith by jerking the broadcaster around and putting them in less advantageous positions. And because of that, broadcasters have suffered.

Senator PRESSLER. Now, Mr. Padden, channel positioning seems to be the stumbling block to must carry at this point. What is the best compromise solution to channel positioning? I know you have mentioned this in your earlier testimony, but what specifically would solve the problem?

Mr. PADDEN. Well, I want to make sure that you understand what is going on right now. In some cases the cable operator takes a local broadcaster out of an advantageous channel and replaces him with a program service the cable operator himself owns.

In other cases, a cable program service comes to the program operator and has the following conversation. They say, look, Mr. Cable Operator, I currently charge you 20 cents a month per subscriber to carry my program service. And if you will give me the local broadcaster's good channel and move him up to the bad channel, I will discount the charge I impose on you by 5 cents, so you will only have to pay me 15 cents a month per subscriber.

The broadcaster cannot get into that negotiating game because the Congress has decreed that the broadcaster cannot impose a charge on the cable operator which he could then discount. We can't discount a charge trying to hold onto the good channel because we are not allowed to impose the charge in the first place.

So, it seems to us that the same body that put us at a disadvantage in this situation, the Congress, has the responsibility to see that the compulsory license you have given the cable people doesn't end up causing us to lose the channel positions we have occupied.

And, Senator Pressler, I would love nothing better than to find a way to bring these negotiations to a conclusion, but I have seen what the cable industry's disingenuous arguments and tactics did in the passage of the 1984 act, and I am determined to see that they do not do the same thing to us in this debate over channel positioning.

Senator PRESSLER. Good. I have some additional questions for the record.

I would just note for the record that where we live on Capitol Hill, we cannot put a dish because it's a historic district. We cannot get microwave because we are behind the Library of Congress, and we cannot get cable because the District of Columbia is so slow. So, while this whole debate is going on, I am totally deprived. I can't even buy it.

Senator GORE. We will see if we can work that out. I don't know.

Just a couple more questions. I wonder, Mr. Padden, if your assistant could put back up the "No cable, no Gretzky."

Mr. PADDEN. We have 8 by 10 reprints if you'd like one, Mr. Chairman.

Senator GORE. I would like one. I have been looking for a Christmas card to send Mr. Malone this year.

Mr. PADDEN. As I indicated, his company is a part owner of the sponsor of this billboard.

Senator GORE. Yes. Now, where is this billboard located?

Mr. PADDEN. It's on Pico Boulevard in Los Angeles, California.

Senator GORE. Now, let's say that I am a resident of Los Angeles, and I am a fan of Wayne Gretzky and Magic Johnson. I want to see these games. But I don't like the outrageous price charged for it. And I look up and I see "No cable, no Gretzky. No cable, no Magic." And it makes me mad. What do I do?

Mr. PADDEN. Other than petitioning Congress to change the 1984 Cable Act I do not think there is anything you can do because the cable industry got it fixed so that nobody can compete with them and they can vertically integrate. They can use their dual revenue stream to bid these rights away from the broadcasters.

When it comes time to bid for the rights, the broadcaster has to figure out what he can bid based on expected advertising revenue. Prime Ticket bases their bid on expected advertising revenue and what they are going to be paid in subscriber fees by Mr. Malone's own cable systems.

Senator GORE. And the company that puts this advertisement up there and sort of rubs it in the faces of the sports fans in Los Angeles gets all of its broadcast programming watched by 72 percent of its subscribers for virtually nothing. Correct?

Mr. **Padden**. All the local signals are essentially free. I believe there is a token payment that has to be made to the tribunal to be in the game, but it is essentially free.

Senator **Gore**. It is essentially free.

Now, if as a consumer I go to look at the franchise for this cable company, and I see that it is granted by my local government, I go to the local government and say, look, I don't like this billboard. It has really made me mad. And more importantly, the price that I am being charged is not fair. I have looked at the cable industry, and I notice that these franchises are selling for more than three times the cost of building them in the first place. And that tells me that there is a 300 percent monopoly rent which any economist will describe as just completely outrageous off the charts. And so, I would like you to regulate their rates and bring them down.

They would say, no, sorry. The Congress has given the cable industry immunity from any regulation. The local government is required to give a monopoly franchise, but then prevented from any regulation of rates at all. That's right. Correct?

Mr. **Padden**. That's right.

Senator **Gore**. I say, well, okay. I have another line coming into my home. The telephone company has a line there. I will go to them and ask them if they can bring me this electronic signal. And they say no. The Congress and the Courts have said you cannot compete with cable. There are two wires coming into your home, but the other one is prevented legally from competing with the cable television company.

So, I go to the broadcaster and I say, well, why don't you bid some more money to get the Laker games back on the broadcast signal. And they say, well, the cable company just has a lot more money to bid because they get our signals for free and resell them, and they get money from their subscribers, and they get money from their advertisers. And so, we can't compete. The structure is such that the cable company has it all: no competition, no regulation, a free source of raw materials, and the right to put up advertisements such as "No cable, no Gretzky."

Mr. **Padden**. Mr. Chairman, I think to be accurate I think there are still some Laker games on broadcast television in Los Angeles. And in that respect the billboard may be false and misleading and maybe we ought to take it to the FTC.

But clearly the trend is that way.

I think there is another thing to notice here. Let's say you woke up in Los Angeles tomorrow and decided that Prime Ticket was charging too much and you were going to go start a cable channel, bid against them for these rights, and then get distribution on the cable system. You wouldn't be able to do that either because you would have to try and go through the leased access provision in which case TCI would charge you for access to the system while their own channel was getting rather than charged, getting fed money from the system. And you would not be in a position where you could compete with their own channel for rights fees because of that economic disparity.

Mr. FRITTS. I might mention, Mr. Chairman, that billboard is not an isolated incident. It is happening all over the country. It is happening with Southeastern, PAC 10, Big 10, Southwest Conference football and Big East basketball.

Senator GORE. Put that other one up there again, the Tennessee-Duke game. Twenty-five dollars per——

Mr. FRITTS. For one game.

Senator GORE. Plus 8 percent tax. I think the ticket to get in the stadium is less than that.

Mr. FRITTS. Preston and I both testified earlier in the week before Senator Metzenbaum's Subcommittee on Antitrust. We pointed out that quite frankly cable is evolving itself into an industry where everybody will have to pay, that they will become the new ticket agent for sports in America. And that is done with the antitrust exemption to major league sports, major league baseball and the NFL. And there are some serious antitrust concerns I think along the way.

But understand that in this instance that they can bid against the local stations by passing through the premiums they have to pay to the consumer, while broadcasters don't have the ability to do that. And consequently if you look five years hence from the Cable Act, I think you are looking at a marketplace that gets further out of balance to the extent that it becomes so inequitable that broadcasters will not be able to compete fairly and bring that programming to the home of the consumers for free.

Senator GORE. Well, you think that we are going to see a lot more sporting events than people now enjoy over broadcast television going to this pay-per-view, this outrageous price per game. Is that right?

Mr. FRITTS. Well, I think the sports franchises have looked at this as their newest and best way to generate additional revenue from those franchises.

Senator GORE. Well, the head of Showtime was quoted as saying that the Super Bowl is going to go to pay-per-view. That statement may have been what attracted the attention of TCI to purchase Showtime. I don't know.

Anyway, let me thank both of you for your courtesy in coming here today and giving such good statements. Thank you very much.

Now, our next panel is made up of Mr. Charles Dawson with C-SAT; Mr. Robert Phillips, the CEO of the National Rural Telecommunications Coop; and Mr. Robert Schmidt, President of the Wireless Cable Association. If all three of you would come up to the witness table. We are delighted to see you here.

If those leaving with the last panel could tiptoe or be quiet anyway, we would appreciate it.

Now, let me thank all of you for coming on this panel. Without objection, your prepared statements will be in the record in full. We invite you to present summaries if you will.

We will start, Mr. Dawson, with your statement. Delighted to see you here and look forward to your words here today. Please proceed.

STATEMENT OF CHARLES DAWSON, C-SAT, CORRALES, NM

Mr. **DAWSON**. Thank you, Mr. Chairman.

I think it is important to point out that I am probably the only witness that is going to be testifying in these two-day sessions of hearings who is not paid to be here. I won't get a paycheck, and that is primarily because—I bring that up because the people that I am here to represent today can't afford a lobby. So, they expect the Senate to simply take the message and be their lobby. So, that is who I will be representing today.

I also will be bringing the goodwill of the Satellite Dealer Coalition and the American Home Satellite Association and every individual satellite organization in our industry except the broadcaster influenced one, the SBCA, who support your bill and ask for the Senate to move S. 1698 and the provisions of mandatory access, third party marketing and the standardized encryption.

I also represent the Satellite Dealer Communication Association of America who represents 1,100 satellite dealers. Those are the surviving dealers under this cartel influence.

They want to bring a level playing field to this industry. They do not want any advantages whatsoever. What they want is fairness, a level playing field. They want to stop the unfair campaigns. Preston Padden just talked about his ad. Well, wait till it goes on for two years.

We have ads running all over the country today that say that these satellite signals are only available on cable. You cannot get them with a satellite dish. They are exclusively available on cable.

Senator **GORE**. Let me ask the staff to get that. I would like to look at that.

Mr. **DAWSON**. And, Senator, even C-SPAN, which obviously is available to every single dish owner, unlike the cable MSOs, is running these lies and distortions that state that their signal is developed and exclusively available on a cable system, implying that there is no other system, wireless, independent or satellite system that could receive the signals. We want to put a stop to that, and this misleading information as you are seeing show up against other industries, like the Independent Television Association just earlier.

I also today am representing over 500 mayors and councils and 5 million cable subscribers who recently in their outrage with the cable monopoly, federally franchised monopoly in this country, who have endorsed and sent this Senate letters of support for movement of the cable subscribers bill of rights which, coincidentally, Senator Gore, has your third party marketing provision in it. So, even the cable subscriber is now starting to see the overall aspect and importance of this conduit of information and how it is being choked up through vertical and horizontal integration of a small number of financial interests.

I today represent the K-SAT and the C-SAT radio station and the K-SAT/C-SAT Army—and that paramilitary term is simply to combat the army of special influence people who daily are afforded the opportunity to visit with their Senators—and the Committee of 435. And they want to send the following message to the Senate today, and they have asked me to deliver it. So, I'm going to do it.

They have been lied to. They have been deceived. The manufacturer of the decoder—at least the FCC has determined that it is a de facto standard decoder, which means you have got to live with it. That's what that means. They have been lied to. They were told that this was the only decoder that would ever be needed for all scrambled signals. That's it. The only one. Of course, three months later it was the only one you need for 95 percent of the scrambled signals.

And, of course, Channel Master has always said it is the only decoder you will ever need. That is a lie. They right now are asking the satellite consumers to pick up the bill at about $150 each for the next—in a series of upgrades which I will explain later I hope. They said this decoder could not be broken. It was compromise-proof. It was secure, and that's why we should not legislate a standard. We don't need one if this one can't be broken. Well, now it is broken, and they are asking the public to pay the bill to fix it. This is absurd. That's the message I bring today.

Obviously, they said the price will come down. I mean, this was the first one in 1986. If they build a couple more and get some volume up, the public won't be paying this outrageous extortion to watch something like a PBS signal.

I am here to tell you that the older models sell for up to $100 more because they are easily compromised. And I am talking about the same day, same place, same model is $100 more than older models just because of the serial number. It is easy to break. And the public has been expected to pay more for the unit that is now in mass quantity building in Taiwan. It's not an American made product. And if you want to get it fixed, you have got to send it to Mexico. I don't know what happened to America in this particular technology. Somehow we got lost.

But we are being asked to pay more for the unit today, the same unit, than we were when we were told that it was the de facto standard and the price would go down. Mark Fowler said I see a $150 decoder for consumers. This marketplace is working. I'd say I can't find it. I'm looking.

If the public is going to be made to switch decoders, which obviously we have already been told we are going to make this switch—we are going to make this switch now. If we are going to be made to switch, let's switch to a standardized encryption form. In other words, let's encrypt satellite signals that have to be encrypted and let's do that through the standard forms that we send transmissions up to the satellite. We do it in a standard way, and we have standards to do that. Let's use an encryption standard that also comes into place with high definition, that has a reasonable life span and can be manufactured by a multiplicity of manufacturers. And there could be a no frills method, a big frills method, and there would be some diversity for consumers. As it is right now, we are going to be asked to pay for the upgrade to the VideoCipher, and I will go on with that if you care to hear it.

Another message I bring from TVRO consumers is that there has been much talk about cable programmers, so-called cable—and that term is totally erroneous. They are satellite programmers who just happened to get cable investors—cable programmers who had their arms twisted and broken and said you either scramble your signal, withdraw it, create a signal blackout to the dish industry—we don't want them as competitors. You either scramble your signal, we'll throw you off of cable. We will bankrupt you. You'll be out of the business, and we will start our own channel to replace you.

Now, there is a lot of talk about the Pat Robertson letter that appeared in 1986 where he says I'm being forced to scramble. The big guys are saying—I am a Christian broadcast network. I want to get my signal out for free to as many people as possible, but I am being told that if I don't scramble, I'll get thrown off.

Then Tim Robertson came up before the Congress and he said, well, Dad was wrong. He was running for President. That was a mistake.

And they also changed the name of the network to the Cable Broadcast Network, by the way, from Christian Broadcast Network. And they scrambled their signal.

I am here to say that I have a tape, the 435 said bring the tape and maybe you, Senator, can hear Pat Robertson say and name names, that he is being arm-twisted into scrambling his signal, which is now a cable signal. And maybe we can send this over to the Justice Department and get some subpoenas, find out exactly who the guy was who twisted his arm, and then maybe throw some of these guys in jail.

Senator **Gore**. This is a tape of——

Mr. **Dawson**. Of Pat Robertson, sir.

Senator **Gore**. On what?

Mr. **Dawson**. On his network just prior to scrambling. He followed it up in writing through his network saying——

Senator **Gore**. Read the relevant portions of that letter if you would.

Mr. **Dawson**. The relevant portion of this letter, sir, says that so by forcing (do it or you're off our cable network), the stations to scramble their signal so there will be continued use of cable.

And in the second paragraph he says we could not take this threat lightly nor presume that the cable company's threat were idle. So, we will be scrambling. And, of course, he says it in his own words.

So, I think that maybe we ought to find out who those bad guys were, put them in jail. And the cable influence which is pervasive over new technologies, it would seem, maybe some of it at least would go away.

I want to call your attention and the Senate's attention to last year when the provisions in the Gore bill were brought up to the full floor. There was a bitter confusion and dispute over the availability of programming to satellite dish owners. And one Senator stood up and said you just call an 800 number and you get hooked up. Well, I don't blame the Senate for saying why are these guys pushing for a bill.

Well, after that hearing, people started calling my radio station and saying where is the 800 number that Mr. Wirth talked about. Well, I had to tell them there is no 800 number for Wrestlemania V. There is no 800 number for the Rolling Stones' concert. There is no 800 number for Tommy and The Who concert. As a matter of fact, there is no 800 number where you just get hooked up.

Now, they told me that without the 800 number, we need the bill. We need the provisions that are in your bill, Senator. We need the mandatory access.

You know, it is bad enough that these cable-controlled programmers have created a deliberate signal shortage to subvert the emergence of American new technology, but they also provide the excuse to steal by refusing to take money from an honest satellite dish owner for the signal. They provide an excuse to steal, an excuse to take them apart. Now, we don't condone stealing of signals, but we also don't condone providing excuses to steal signals.

Your mandatory access provision—and hopefully with working with Senator Danforth we can provide that mandatory access provision and third party provision like is in your bill. Your mandatory access provision, Senator, would remove the excuse to steal satellite signals. It would also send a clear message to every person with a satellite dish that you can be legal in the use of your satellite dish. The Senate codified legality of use of the satellite dish. What it hasn't done is codify the legality of getting the signal. So, we need the mandatory access provision so that we can do away with the theft of service or at least the excuse. Then we will go out and catch the bad guys that have been stealing the signals.

You know, if you are wondering where the volumes of dish owners, all the calls and the letters and the telegrams have gone, because a lot of them have disappeared, I am here to tell you that these people have lost faith in the system. They have gone away. They have made the decision that the Senate, the Congress, the FCC should have acted by now. I want to send a message to them that, look, I brought that message before this committee. They were kind enough to hear me and listen.

Let's have the Senate send a message back that they lost faith too soon. The system does work. It is hard for the person who sees the "no Gretzky, no Magic, no cable" sign or the only on cable availability of programming—it is hard for them to have faith in a system that doesn't do something about these lies and distortions in the marketplace. Send the message that the system works, have the Senate pass the third party access, mandatory access, standardized encryption provisions in the Gore bill in conjunction with the Danforth bill, and let's go on to competition.

You can do it for competition. You can do it because you believe in the American system. You can do it because it is the right thing to do. Most of all, you can do it for your children and my children because that conduit of information, that free flow of information, that access to information in this country, that constitutional right is right now in the grip of a cable cartel in over 60 percent of the American homes.

And the camera that is filming me right now is controlled by a cable cartel. If it were a major oil company cartel that owned that camera, we would do something about it tomorrow morning. We'd say, well, they could have the capability of censoring Mr. Dawson's comment from the people he represented. But it's a cable cartel that controls it right now, and they control it all the way down into my mother's home. And we will talk about that price disparity and the ability of a satellite dealer to serve my mother.

So, please heed the message that we have brought you, and we really thank you for the opportunity to give you that message.

[The statement follows:]

STATEMENT OF V.C. DAWSON

Good day, Senators. I think it is important to let you know that I am probably the only person who will not get a paycheck for being here before you today. I am a messenger. I bring you a message from over six million cable subscribers, five-hundred mayors and counsels that have endorsed the "Cable Subscriber's Bill of Rights", which calls for the third party non-discriminatory programming in S. 1698, the Gore bill, and almost five-hundred towns and cities. Also, the Satellite Dealer Coalition (SDC) and the American Home Satellite Association (AHSA) support passage of S. 1698. All industry associations, with the exception of those that are programmer influenced, support this legislation.

I today represent the Satellite DEALER Communication Association (SDCA) and their 1100 dealers that want a level playing field to compete. They also want to bring to an end subtle knock-out tactics like video channels advertising that they are "only available on cable". Even C-SPAN has participated in the lie that it's signal is not for dish owners. They also insulted the dish owner by running this "cable only" message on the satellite.

I represent today that K-SAT/C-SAT Committee of 435 and the K-SAT Army. Their message is that they have been deceived by the manufacturer of the so-called "defacto decoder".

They said it would be the only one you would ever need. Now, they want you to spend $150.00 to upgrade.

They said it could not be broken. Now, they want the public to help catch all the breakers.

They said there would be price reductions. Yet, a stand-alone costs dollars more now than it did the day it came out. Older models demand higher prices as evidenced by these two invoices.

If the public is to be made to switch decoders, let's switch to a satellite encryption high definition standard that could have a reasonable life span. As it is, we switch from the VCII to the VCII Plus. The next switch is to the VCII Plus HDTV and so on. Contrary to what you've been told, there is no compatibility between the defacto standard VCII and this new VCII Plus.

Another message that I bring from the TVRO consumer is that there was much talk, and even a Justice Department investigation, over whether programmers were being arm twisted or threatened to scramble their signal. Everyone singled out Pat Robertson's letter stating that he was being forced by cable to scramble. (Attachment R-1). Later, his son testified that it was not true. The K-SAT Army wants you to know that it is true and asked me to deliver this tape to Mr. Robertson of CBN, now the Cable Channel, stating that he was being forced to scramble or they would throw his channel off, leading to instant bankruptcy. Here is the tape. Maybe you Gentleman can get the Justice Department to issue a subpoena and we can find out which cable companies twisted his arm and throw them in jail. Maybe that would put an end to their conspiracy of influence.

I'd like to call your attention to last year's vote on access third party programming on the Senate floor. You were all told by a Senator that there was an 800 number we could call and get all the programming. (Congressional Record, October 7, 1989, Pages S.15136–15137). Well, we voted down the bill and the public figured, without the bill, they needed the 800 number. They started calling me. I told them to call the Senators who said we didn't need the bill because of Senator Wirth's 800 number. Where was the 800 number for Wrestlemania V—The Who Concert production of the rock concert "Tommy"—The Rolling Stones Summer Solstice '89? Well, there is no such number, so we need the bill.

By the way, we have noted that the same cable interests or controlled video programmers who refused money for their programming from legal dish owners in 1980 are refusing access still. Here is a list of some non-legally accessible programs to dish owners. It would seem that they like to make people pirate the shows. The mandatory-access provision would make it legal to buy the programming, removing this artificial signal shortage, curtailing signal theft.

It's bad enough that the cable controlled programmers have created a signal shortage. This bill, Senators, would removes both the signal black-out and the excuse to steal. There are two people who benefit on the theft of these signals. The decoder manufacturer and the pirate. Let's remove any excuse to steal. Give equal access to competing technologies. Move S.1698.

If you are wondering where the volumes of phone calls, letters, and people have gone on this issue, they have lost faith in our system. They expected a solution from you before now. I've done my job, I brought you the message.

Senators, you can send those volumes of people a message. You can let them know they lost faith in the system too soon. Send the message. Pass S.1698. Reregulate and bring competition to the cable cartel. Do it for the free flow of information. Do it to support capitalism and free enterprise. There are a lot of reasons to do it. One is that they control that camera right over there and your next words and actions through it. Thank you.

BRIEFING PACKAGE

This information is supplied by the following:

The Satellite DEALER Communication Association (SDCA), which consists of over 1100 dealers nationwide. Several dealer organizations unified to form the SDCA. These included the Home Satellite Television Association, the USIA, and the members of the K-SAT Quality Dealer Program.

The Satellite DEALER Communication Association/Consumer Action Committee (SDCA/CAC), a group of consumers under the umbrella of the SDCA—who share a common goal with the SDCA—the passage of positive TVRO legislation.

The K-SAT/C-SAT Committee of 435, a legislative TVRO action group. Also known as the K-SAT/C-SAT Army, they are a grassroots group of satellite dish owners from all walks of life who are associated with a satellite-delivered radio channel (formerly K-sat; now, C-SAT). The term "army" was coined by its founder to combat the "army" of special interest cable lobbies throughout the USA. Their goals are the same as the SDCA and SDCA/CAC. The "435" stands for the 435 Congressional Districts. The members of the various districts keep the Representative of that district informed about TVRO legislation. During the last four years, Congress has received numerous letters, telegrams, phone calls and visits from the K-SAT/C-SAT Committee of 435 members.

In fact, lack of non-cable programmer distributors, lack of access to programming, the monopoly manufacture of the descrambler, and the effect lack of competition to cable has had on the cable subscriber were the same problems the Committee of 435 were fighting four years ago. They have been joined by the SDCA and the SDCA/CAC. Each of these issues will be addressed separately.

ACCESS

One of the primary problems that exists today is lack of access to programming. Testimony presented to Congress by programmers and the manufacturer of the descrambler (General Instruments) has inferred that satellite dish owners have access to all programming through a single 800 number. This is not factual and, indeed, the dish owner has been denied access to several programs because of the delivery mechanism discrimination (satellite VS cable). Some of the more recent events include The Who Concert "Tommy" in August, 1989; Titan Sports/World Wrestling Federation's presentation—Wrestlemania 5; and the *Grateful Dead* Summer Solstice '89 in June. The *Grateful Dead* concert ad says "Only on Pay Per View Cable TV".

The primary reason given for denying dish owners access is because the descrambler is not secure and the programmers are afraid that if their signal goes through an authorization center dish owners will be able to "pirate" the signal. What they don't realize is that the legal dish owner won't be able to "pirate" it and the illegal dish owner can "pirate" it whether it goes through an authorization center or not! This is why honest consumers become illegal consumers. They try to deal within the system to get the programming they want and, when that fails, they turn to piracy. Lack of access is probably the largest incentive for the consumer to seek out a modified decoder.

Those profiting from piracy are the pirates, General Instruments and even some distributor members of the SDCA, as evidenced by a communique to the SBCA from the SDCA concerning one GI distributor.

Why do programmers deny access to satellite dish consumers? Vertical integration now exists between programmers and cable and this gives a big advantage to cable. Cable does not want satellite dish owners to receive the same programming as cable consumers, thereby competing with cable operators. This is evidenced by the "Only on Cable" advertisements that have been appearing lately. Cable is sending the message to the cable subscribers that cable is the only one who can supply them the programming.

LACK OF THIRD PARTY NON-CABLE PROGRAM SUPPLIERS

Last year the National Rural Telecommunications Cooperative was heralded as the major "breakthrough" in third-party programming packages. At the June 21, 1989 hearings before the Subcommittee on Commerce, Science, and Transportation, United States Senate, Bob Phillips testified that the NRTC "breakthrough" was not really a breakthrough. He brought up several points that indicated that there are still no non-cable third party distributors to the home satellite dish marketplace. Bob Phillips testified that the wholesale price of programming to the NRTC was an average of 444% higher than the wholesale price charged to independent cable operators for the same programming. These differences ranged from 167% to 790% higher than cable wholesale prices. The NRTC said the reason was because of the horizontal and vertical integration of the programmers and cable.

American Movie Classics (AMC) is 50% owned by TCI. The NRTC was offered AMC for $1.00 per month per subscriber but only if AMC was included in a Rural TV basic package. At the same time, AMC sells to cable for $.35 per month per subscriber without any such conditions for inclusion in a basic package.

Superstation TBS, uplinked by Southern Satellite Systems, Inc., a subsidiary of Tempo Enterprises, Inc., which is 100% owned by TCI offers their programming to cable for $.04–$.10 per subscriber per month, but will only sell it to the NRTC for $.78 per month per subscriber.

TNT (Turner Network Television) is not available to the NRTC, but is sold for distribution through local cable operators or TCI (Netlink) to the home satellite dish market. This insures that cable will maintain control of the product and prevent competition.

TCI is now arranging to purchase 50% of Showtime Networks, Inc. Showtime Networks, Inc. is a major distributor of programming to the home satellite dish market as well as a major programmer. This will further erode competition in the marketplace and give cable more control over the home satellite dish market. Talk of TCI and Showtime combining their TVRO marketing operations is even more troublesome.

Artificial boundaries for distribution of programming is for the protection of cable technology. Satellite technology actually knows no boundaries and the demands placed on the NRTC and others trying to enter the programming distribution market are to insure cable's control. The fact that cable places such boundaries on those who would like to become a programming distributor shows that there are still no third party non-cable distributors of satellite delivered programming available. Cable continues to control all distributors either through vertical integration or territorial restrictions.

Currently, the best available package price for thirty-five basic channels is $29.12. This works out to an average of $.83 per channel per month. According to the figures of the GAO report on cable pricing submitted before the House Telecommunications and Finance Subcommittee on August 3, 1989, the average price to the cable subscriber is $.46 per channel per subscriber per month. This represents a 100% markup at the retail level with all of the additional profits returning to cable interests.

Because of the disparity in pricing of programming, plus the capital expenditure necessary by the home satellite dish owner, cable continues to be able to raise rates at an alarming rate. There are simply no competing market factors to keep cable rates in check. When Congress passed the Cable Deregulation Act of 1984 and legalized the reception of home satellite dishes it was understood that home satellite dishes would be one of the competing market factors controlling cable subscriber prices. This has not happened and the home satellite dish market has not been allowed to compete with cable. For this reason, almost 500 cities have passed the Cable Subscriber Bill of Rights urging Congress to allow the cities to regulate cable or offer some sort of competition. The satellite industry could be that very competition, but it will require the intervention of Congress to allow it to enter the market, as cable will not allow it. While we are not asking that Congress reregulate cable, we do ask that it make allowances for competition in the marketplace and pass legislation to allow the competition to exist on a level playing field.

MONOPOLY CONTROL OF DESCRAMBLER TECHNOLOGY

In the field of decoder technology, there continues to be numerous problems because of the monopoly control by General Instruments. These problems include the inability of General Instruments to insure the security of the technology, the obsolescence of the decoder because of the inability to secure the technology, the high cost of decoder modules, with reverse economics affecting the cost of decoder modules, and the previous testimony before Congress by General Instruments outlining what the decoder can do, but which has never been fulfilled.

Forbes magazine (June 29, 1987) reports General Instruments stock soaring from 16 to nearly 37. According to Forbes, "One reason is the electrifying profit margins on the VideoCipher II, which run over 35%". These are net margins after overhead and the cost of marketing.

In early testimony before Congress, General Instruments continued to deceive Congress that the decoder technology was secure and had not been compromised. Later, General Instruments admitted that there was a breach of security, but that they could turn it off at any time. After demonstrations in Washington, D.C. by the K-SAT Army, the Committee of 435, and the Home Satellite Television Association, showing that the decoder had been compromised and demanding that General Instruments turn off the illegal units, General Instruments finally admitted that they had a problem. Rather than trying to make the module tamper proof, which would not serve in the best financial interests of GI, they initiated several software programming updates. Had there been competition in the marketplace, other manufacturers may have been able to secure the actual housing the descrambler was housed in. Instead, General Instruments was allowed their monopoly status to manufacture the compromised units until the profits were maximized. Now, the decoder will be scrapped and a new decoder, (a redesigned Starlok Decoder which GI originally designed as a competitor to M/A-Com, the original designer of the VideoCipher), the Video Cipher II Plus will be introduced. Programmers have already begun to switch to the new system while leaving the old system running. General Instruments is being allowed to switch decoder technology without scrutiny because of the monopoly status granted to them by an agency of the Federal Government, the FCC.

With the change in scrambling methods, the legal subscribing consumer is expected to pick up the expense of the descrambler change-over. The price to the consumer who wishes to become an "early adapter" is $129.00. Allowing General Instruments to completely obsolete technology at will is the same as giving them a license to print money without having to approve it through any regulating authority. General Instruments will be able to experience a Two-Hundred Fifty Million Dollar windfall from the change-out of encryption technologies.

When will General Instruments turn off the old decoder system and force consumers to go out and purchase new decoders? There are no set dates established for this to happen. We ask you to consider if you were a merchant and everyone in the community had keys to your store, allowing anyone to come in and take what they want. Even though only 70% of the citizens would use the keys, how long would it take you to call in a locksmith and get new locks installed? Today, most satellite dish owners hear of where they can find the key and nearly 70% have gone out and got a copy of the key. The programmers know that General Instruments has chosen not to have the locks changed up until now because everyone had to purchase the key blanks (descrambler) from them. Now, General Instruments will be allowed to change the locks and go out and sell the key blanks all over again. General Instruments could have solved this problem four years ago, but they chose not to because of the financial gains they could make by not sealing the descrambler modules. It should be noted that they currently do not plan to make the new decoder module more secure through sealing the unit. The consumer is expected to pay for the lack of integrity of General Instruments to make their product do what it was intended and advertised to do. That was security to the programmers.

It is time for Congress to act. It is time for Congress to remove the control of the competing (satellite) technology from cable's grip.

Justice delayed is justice denied.

Senator GORE. Thank you very much.

I might just say that I think the C-SPAN service is the best single thing the cable industry has done, and never once have they attempted to control the content of the signal at all.

And I share the sentiments expressed by Senator Ford yesterday that I wish more cable systems would carry C-SPAN. I think it is a great service.

I also want to express admiration for your message to satellite dish owners to keep the faith because the system does work. It sometimes moves way too slowly. I thought it should have moved four or five years ago to solve this problem. Some things take time, unfortunately. But, boy, things are changing now. They are on the move now.

So, thank you very much, Mr. Dawson. We will have questions in a moment.

Our second witness is Bob Phillips, the CEO of the National Rural Telecommunications Cooperative. We are delighted that you are back, Mr. Phillips, and we look forward to your statement.

STATEMENT OF BOB PHILLIPS, CHIEF EXECUTIVE OFFICER, NATIONAL RURAL TELECOMMUNICATIONS COOPERATIVE

Mr. **Phillips**. Thank you, Senator. NRTC is the National Rural Telecommunications Cooperative, and it is an association of 557 rural electric cooperatives and rural telephone systems. NRTC is committed to providing access and affordable television programming to rural households, and today we are bringing home satellite service to thousands of rural customers.

When Congress acted to deregulate cable, no one envisioned that it would develop into the highly concentrated industry that it is today. Based on our experiences since that 1984 act, the act needs to be reexamined, and the cable industry also needs to be examined very closely. It is our view that Congress has two options: either regulate cable or provide effective competition. There is no effective competition for cable today.

In my previous testimony, I have outlined in detailed documentation for this subcommittee about our experiences as a non-cable distributor to the home satellite dish marketplace. The abuses that I described then continue today. Things have not changed.

From our utility perspective and our 50 years of experience in providing a stable service to consumers, we see patterns of cable control without conscience, rates that are out of reason and selfish greed before service.

Yesterday in his testimony, Mr. Mooney told you that programmers see an opportunity for better margins in this home satellite dish market. Well, we know that is true. We pay 444 percent on average more than what a small cable operator would pay for the same signals. These rates are not justified by costs. It is pure opportunism. Mr. Mooney said it himself that they want a higher margin. And where does that margin come from? Well, it comes from rural consumers, dish owners.

In addition, NRTC and other non-cable distributors can't even gain access at any cost to some programs. Yesterday this subcommittee was asked to applaud the fact that CNN and Headline News are a foreign export. Well, I am here to tell you that Turner's new service, Turner Network Television, is not even available to our rural consumers at any cost.

In addition, Viacom has filed an antitrust suit against HBO, and they are claiming that HBO is engaged in exclusionary and anticompetitive behavior against them for denial of access. Yet, Viacom's services, Showtime, the Movie Channel, MTV and VH1, aren't available to any non-cable distributors for the home dish market.

Notice these services are vertically intertwined with cable ownership. And now that TCI is pondering acquisition of half ownership of Showtime networks, they are going to be even more concentrated.

The competitive barriers of price discrimination and denial of access to distributors serve the interests of cable, and the result has been clear. This home satellite dish market is floundering as a cable competitor and also as an effective delivery technology for rural America. The result is that rural Americans are remaining at a distinct disadvantage in a maturing information age.

We are also urging you to examine closely KU band and the potential of high power, direct broadcast service. These are potential competitors to cable. But as we are here today debating these issues, Mr. Malone and his other MSO friends are meeting to decide whether or not they should buy all of the available KU capacity. Those are the industry reports that I have from the press yesterday. So, the cable industry wants insurance against any competing technology.

Mr. Chairman, we believe that Congress must act now to ensure that cable has effective competition. There are 2 million dish owners in this country that need your assistance, and we are recommending the following: mandate equal access to programming on technology neutral terms, conditions and price; restrict cable monopoly control of both the ownership of the content, which is the programming in this case, and the conduit of information, whether it is a home backyard dish, KU band or MMDS. And finally, I would also urge the subcommittee to enlist the FCC's assistance by directing the commission to exercise responsibility over the healthy development of the home dish marketplace.

Thank you.

[The statement of follows:]

Statement of Bob Phillips
Chief Executive Officer
National Rural Telecommunications Cooperative

Hearings Regarding the 1984 Cable Telecommunications Act
Communications Subcommittee of the
Committee on Commerce, Science and Transportation
US Senate
November 17, 1989

Thank you, Mr. Chairman and members of the Subcommittee. My name is Bob Phillips. I am the Chief Executive Officer of the National Rural Telecommunications Cooperative, a national organization of 557 rural electric and telephone systems serving the sparsely-settled areas of the United States.

NRTC is committed to providing access and affordability of television programming to rural households through the home satellite dish. As I've testified in previous Congressional hearings, satellite delivery technology is ideally suited to serving rural America, where an estimated 20 to 30 million consumers suffer poor off-air television reception and will never receive hard-wire cable television.

With Congressional support, NRTC's has made progress in bringing home satellite service to rural areas. NRTC's "Rural TV" package contains 12 basic scrambled services plus another 23 scrambled services available as premiums, and optional channels. Since Congress assisted us in June of 1988 obtaining distribution rights to several popular program services, our subscriber base has grown four fold.

Still, NRTC is extremely concerned that rural Americans today do not realize the full potential of satellite technology. I welcome the opportunity to discuss our concerns about the concentration of ownership in the cable/programming industry. This concentration, we believe, is the main reason that the home satellite dish industry is not developing despite the high level of interest we know exists. The main factors preventing the development of a healthy industry include:

> 1. cable programming is not available to distributors on fair and non-discriminatory terms when compared to cable. In fact, some cable programming is not available at any price to non-cable distributors;
>
> 2. cable affiliated satellite carriers who benefit from a compulsory license for the dish market blatantly discriminates against distributors serving the home dish market; and
>
> 3. the control exerted by cable in the home dish market coupled with a flawed descrambling technology has caused a serious piracy problem which threatens the life of this technology as a practical distribution method and thus its promise as a cable competitor.

Based on our experiences in the distribution of programming to the rural home satellite dish market, NRTC believes that the Cable Telecommunications Act of

1984 should be examined closely, with special emphasis on the effect of the concentration of cable ownership in the market and on the development of non-cable technologies. We believe there is cause for concern and we believe these hearings are prudent in light of the dramatic changes which have occurred since the Act was passed.

Despite our concerns about the status of the cable industry today, we believe that Congressional actions in the past have been in the best interests of the urban and rural consumer. The passage of the 1984 Cable Telecommunications Act legitimized the home satellite dish marketplace and allowed this delivery technology to bring benefits of the information age to the vast rural reaches of this nation.

And were it not for Congressional support, NRTC would not have gained a toe-hold as the first independent third-party distributor in the delivery of satellite television service to rural subscribers. We see this support as a continuation of the 50 years of Congressional support of rural Americans through the rural electric and rural telephone programs. Your support in the provision of universal utility service to the distant reaches of the nation have meant a better life and opportunity for millions.

The years to come will see the often heralded "Information Age" come to pass and the delivery of its benefits will depend on the technologies addressed at these hearings--from cable to fiber to satellites. It is imperative that Congress and the Federal Communications Commission assure that all Americans, regardless of where they live, have access to the Information Age. Congressional support of "universal television service" will assure that rural America participates in the Information Age.

Mr. Chairman and members of the Subcommittee, we believe that when Congress acted to deregulate the cable industry it did not envision the cable industry evolving into the highly concentrated industry it is today. But at this time all evidence suggests that adequate assurances from Congress are needed to encourage competition from "like" cable services such as home satellite dish, MMDS, and SMATV.

We believe that Congress has two options: either return the cable industry to rate regulation (which does not address these possible competitors) or, rather, Congress should take action to encourage cable industry competition by:

1. providing access to cable programming on a technology neutral basis and;
2. providing the necessary safeguards to ensure that monopoly cable providers do not control both conduit (the hard wire, satellite, MMDS, SMATV,etc) and the content (programming).

There is no question that the cable industry has abused its monopoly position to thwart competition from alternate technologies by controlling access to product, price and territories of service. In my testimony of June 21, 1989 before this Subcommittee, I presented many examples of NRTC's experience as a new entrant in the home satellite dish marketplace. The abuses which I described then continue to exist:

o NRTC's wholesale cost for the 17 channel Basic Plus package is 444% higher than what a typical independent cable operator pays. This disparity for individual programming services ranges from a "low" of 167% to a "high" of 790% As an example, the TCI-owned Tempo Enterprises Inc. uplinks and distributes, through its Southern Satellite Systems, the popular Superstation TBS. Even small cable systems can acquire TBS for 10 cents per consumer per month. NRTC must pay 90 cents per consumer per month. This nets Tempo 78 cents when the statutory copyright payment is taken into account.

o NRTC cannot gain access to all scrambled satellite programming for distribution to Rural TV subscribers. Turner will not sell TNT to NRTC or any other non-cable distributor. Viacom Satellite Networks, the largest single marketer of programming to the home dish market, refuses to sell the MTV Networks, including MTV, VH1, Nickelodeon, and Showtime/The Movie Channel to non-cable affiliated distributors. (NRTC was granted limited distribution rights to Nickelodeon as part of the June 30, 1988 contract "breakthroughs", but NRTC still cannot gain distribution rights for the other programming services.)

o Negotiating for distribution contracts with programmers which have close cable ties is always much more difficult than working with programmers that have greater independence from cable and cable ownership and investment. Showtime Network's 50% acquisition by TCI is a further example of concentration of control and ownership in the cable/programming industry.

Consider TCI, the nation's largest cable MSO. TCI is following its strategy of dominating the market through its step-by-step purchase of competitors. It currently controls its own TCI Satellite Service, Netlink USA, Tempo Satellite Service, it also has ownership interest in Turner Broadcasting Network's direct to home authorization center and may soon increase its involvement with Viacom Satellite Networks.

Showtime's and TCI's home dish satellite distribution services now reach more than 65% of the US home dish market. Showtime is the #1 program packager and TCI's three home dish marketing arms are #2 program packager. By combining Showtime and TCI, the focus of the conduit and the content in one entity should give pause to anyone interested in a competitive marketplace.

Cable's interest in controlling competitive technologies and its greedy price gouging appear to be the only reasons for the wholesale price disparity between cable and the home dish market.

If the answer to this problem of ownership concentration means that cable should divest its ownership of programming, or if it means that cable should be excluded from competing in the home satellite dish marketplace (in the same way Congress excluded broadcasters from competing in the cable marketplace), then so be it. The answer is particularly important in areas where cable does not and will not serve --rural America.

We know that Congress is concerned about these trends. Hearing after hearing on the topic has been held and bill after bill has been introduced.

We know that the FCC is concerned. Chairman Sikes testified at FCC Reauthorization hearings that "A key FCC role is to maintain both the perception and the reality of marketplace fairness."

We know that both members of this Committee and Chairman Sikes are sensitive to the issue of extending "Information Age" technology and access to service to the reaches of rural America.

To that end, last year Congress passed the Satellite Home Viewer Act (P.L. 100-667) which granted a compulsory copyright license to satellite carriers for the right to retransmit superstation and network signals to the home dish market. In addition, Congress placed an obligation upon the carriers to provide nondiscriminatory service to distributors serving the home dish market. The FCC was directed to prepare a report to Congress on whether satellite carriers unlawfully discriminate against distributors of home dish programming. Congress recognized that the FCC had the regulatory authority to adopt rules necessary to prevent such discrimination.

NRTC has presented detailed comments in this FCC proceeding by providing specific instances of unlawful discrimination by satellite carriers. The carriers have not disputed our price disparity figures, nor have they presented evidence of increased costs to serve the home dish distributors like NRTC. Rather, they have argued that the home dish market is unlike the cable market and as long as they charge all home dish distributors the same, albeit high, price, it is nondiscriminatory. We do not agree.

And we do not believe this was Congress' intent when it passed the Cable Act. Nor do we believe this is the kind of "fairness" that Chairman Sikes and the FCC should accept today. We are anxious for the FCC to issue its report at the end of the year. If the FCC finds that satellite carriers cannot lawfully continue to discriminate against home dish distributors as compared to cable distributors and it acts to remedy the situation, no further Congressional action regarding satellite carriers should be necessary. However, Congressional action will continue to be needed to address cable programmers' control of the home dish market.

In our submissions before the FCC, NRTC pointed out that the FCC has the regulatory authority, under Section 202(a) of the Communications Act of 1934, to prevent carriers from making "any unjust or unreasonable discrimination in charges, practices, classifications, regulations, facilities, or services for or in connection with like communications service, directly or indirectly, by any means or device..."

NRTC believes that wholesale programming service to the home satellite dish market is a "like" wholesale programming service to the cable market. In all of our previous testimony we have demonstrated that the services are identical and have no functional differences whatsoever. Senators Gore and Pressler have introduced legislation that will address these issues. We support their enactment.

The 1984 Cable Act envisioned the encryption of satellite signals. The FCC is now engaged is an inquiry to determine the need for a universal encryption standard for the home dish market. However, NRTC does not believe the FCC's inquiry goes far enough. We support the language introduced by Senator Gore which would act to protect those legitimate home satellite dish viewers who have purchased General Instruments VideoCipher II technology. Industry sources indicate piracy levels are now 60 to 85 percent. It is clear that VideoCipher technology has been compromised and General Instrument is now moving to a "more secure" version called the VideoCipher II "Plus," but at the customer's expense.

We sincerely believe that the FCC must exercise its regulatory oversight in this matter. Legitimate consumers must not be left with useless equipment or with another charge, this time for $129 to upgrade their existing VCII modules to VideoCipher II Plus. The failure of the VideoCipher II technology is the responsibility of General Instrument. (Summaries of NRTC's comments in the FCC proceedings applicable to the home dish market are attached. NRTC would be pleased to make full copies available upon request.)

If left unchecked, unfair programming prices and forced equipment upgrades will continue consumer confusion about the home dish marketplace and will fuel rampant piracy which threatens to destroy the entire home dish marketplace and the investment made by 2.4 million Americans.

This would result in clear winners and clear losers. The winner would be the cable industry with one less competitor. The losers would be every rural American left without Information Age access.

Mr. Chairman and Subcommittee members, NRTC is committed to fairness in access and service to rural America. Our members have demonstrated this commitment through their track record of successful universal electric and telephone service to America's rural reaches.

From our utility perspective and 50 years of experience in providing stable service to consumers, we see patterns of cable control without a conscience, rates out of reason, and selfish greed before service.

I have outlined our proposals in this testimony. In brief, the home satellite dish market problem is clear:

- o the home satellite dish market is floundering as a cable competitor and an effective delivery technology for rural America;
- o concentrated cable power is the major factor in the downfall of the dish industry through cable's programming control;
- o rural Americans remain at a distinct disadvantage in the maturing Information Age;
- o Congress must act to insure that cable has an effective competitor and that rural Americans are not left behind.

The time for Congressional response to this abuse of the Cable Television Act of 1984 is now. Mr. Chairman and Subcommittee members, NRTC believes three things must be done to bring balance and competition back into the video distribution industry of our great nation. They are:

1. Mandate equal access to programming on technology neutral terms, conditions and pricing.
2. Restrict cable from control and ownership of both the content and the conduit of information to rural America.
3. Provide regulatory oversight of encryption technology.

Many areas of rural America have not seen improved television selection or reception in thirty years. Rural consumers that received one or two channels in the '50s, often receive the same limited channel selection today.

But consumers are aware of the changes in television. They know that a great and growing selection of programming is available in heavily populated areas that can have the economics to support program delivery. But in the consumer's mind, that is not the issue. Universal television access is the issue.

The consumer does not care if their programming is delivered by cable, satellites, or microwave, roof antenna, or fiber. They care about access and they care about price. And that is what Congress should address, non-discriminatory universal access to affordable programming.

NRTC stands ready to assist Congress in any way possible to bring Information Age access and competition, fairness and equality to rural America.

I thank you for your invitation to speak and for your attention.

Senator GORE. Thank you very much.

Our final witness on this panel is Robert Schmidt, President of the Wireless Cable Association. Welcome and please proceed.

STATEMENT OF ROBERT L. SCHMIDT, PRESIDENT, WIRELESS CABLE ASSOCIATION

Mr. SCHMIDT. Thank you, Mr. Chairman.

This is, indeed, a welcomed opportunity to testify. In just the last two hearings, cable interests have testified before the subcommittee for over six hours. Mr. Mooney can afford to submit 100 pages of testimony and hire professors to write studies. And as someone noted yesterday, he has been doing this, saying the same thing for two or three years.

He says trust us. Cable will clean up its own house. But yesterday I read in the "Wall Street Journal" that Mr. Mooney doesn't think there is a problem. He says that the Danforth bill—and I quote—"offers a series of extreme solutions to problems that are either modest or nonexistent."

So, I think the story changes depending on the circumstances. I am glad to appear today with a different message. Deregulation without competition will not work.

Wireless cable was created by the FCC to provide competition, multichannel competition, to cable. Today wireless cable is ready to compete but it can't. It can't get the programming needed to enter the market and serve consumers. I would amend that statement to say we are doing it in spite of major barriers to entry.

Yesterday when TCI's John Malone appeared before the subcommittee, no one mentioned the article about him that very morning in the "New York Times." As it was mentioned earlier, I would suggest that that article be submitted as part of this record.[1]

I think it is a very interesting article. I think it is very revealing. It says we are "hungry for programming." And if you don't appreciate the need that any competitor has for programming, then I suggest you read Mr. Malone's statements again.

I have had conversations about some of the activities of TCI recently, and I talked with a gentleman who has some relationship to the company. I said, "what do you want me to say about this latest proposal of TCI to buy 50 percent of Showtime?" And he said, "trust us, we are going to get programming to the wireless cable industry."

I said, "should I just dust off the comments that I made in the House Judiciary Committee hearings on the Time-Warner merger. What assurances are you going to give us?" He said, "trust us, we are going to get programming to wireless cable."

I want to trust TCI. I want to believe Showtime. But evidence is to the contrary.

If you have any doubt why access to programming is crucial to the survival of the satellite television distributor, again just read the N.Y. Times article. If you have any doubt what motivates TCI, read the article.

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[1] See New York Times, Nov. 16, 1989.

I understand that yesterday there were very strong indications that legislation is coming. I urge the subcommittee, that as the legislative effort moves forward, that competition be part of the legislation.

I urge the committee to keep competitors, such as wireless cable, in the bill.

Access to programming is a critical issue. There have been suggestions in Mr. Mooney's testimony that there is no problem. There is a "study" that they funded by a Dr. Klein—well I refer to that as a public relations proposal when you hire somebody to write a study that says what you want it to say it is public relations. I have taken issue with that study from the day that I saw it presented in the Senate Judiciary Committee hearing.

The bottom line is we generally do not have access to what I call the crown jewels. We do not get Showtime. We do not get HBO. We do not get ESPN, and we certainly don't get TNT. And to add to that list, we don't have access to regional pay sports networks.

I found very interesting the dialogue in the previous panel concerning the Los Angeles pay sports network, Prime Ticket. I would like to submit some additional documents for the record, but I would just like to read briefly from the documents.

I am submitting for your files a series of correspondence between the wireless cable operator in Los Angeles, who has been seeking programming from Prime Ticket. The individual, who is a vice president of wireless of Los Angeles, has been writing the president of Prime Ticket for about seven months receiving no answer.

Finally, being frustrated, he chose to write Mr. Bill Daniels, the chairman, and just said, please, "I have sent numerous follow-up letters and have placed many unreturned calls. I would appreciate your advising me as to who I should contact to discuss Wireless of Los Angeles' affiliation with Prime Ticket."

Now, he gets a letter back from the president. "Dear Mr. Ruppe: Thank you for expressing an interest in becoming affiliated with Prime Ticket Network. At this time, we are not interested in offering our service to Wireless of Los Angeles."

So, in a good, persistent follow-up, he writes back what do you mean by "at this time?" What circumstances change that?

The answer: "Dear Mr. Ruppe, This is in answer to your letter of October 23rd regarding clarification of the phrase 'at this time'. This phrase means not now, and I will contact you if the time arrives."

"Thank you for your continued interest in Prime Ticket Network."

So, we have heard in previous testimony of Mr. Mooney that there isn't any evidence that we are being discriminated against. There isn't any evidence—the system is working. What's the problem?

Now, I really believe that there are three reasons legislation is needed.

One, large portions of the United States will never be wired, and this speaks to the gentlemen seated with me today. There are 20 million homes in this country who I think are headed for what I call the have-not list.

And wireless cable is doing some things in rural America that I think are very important. I turned on a system 10 days ago in South Dakota, and that system is serving people in rural Sioux Falls, Yankton, Mitchell, South Dakota. These people haven't been able to get any programming. Some of them invested in dishes and then ran into the same problems the other gentlemen spoke of. We are now delivering them product.

We don't have HBO. In some instances we do get ESPN, but they red-line us. And if you are not familiar with the term, basically what it amounts to is they ask us for the ZIP codes in the area in which we are going to serve wireless customers. And then they write us a letter and say we are happy to grant you this agreement with the understanding you don't serve the following ZIP codes. That letter was written to the folks in Los Angeles. And when they eliminated the ZIP codes that they were not able to serve, they were entitled to serve 10 percent of the market. So, in effect, it is a territorial protection that they are looking to do with this process.

Second, cable controls programming. No one else in the present situation can start programming on their own.

Third, cable won't clean up its act itself. I found it very interesting. Dr. Malone, who I think is a very brilliant man, but he made it very clear—and I have to paraphrase his remarks--when he testified in the House last May. Dr. Malone in so many words said as he pointed to the panel of the House Energy and Commerce Committee, ladies and gentlemen, my job is to do everything I can to get a return on investment for my stockholders. As I see it, it is your job to look at public policy, and if public policy isn't right, change it. Until you change it, I am going to do everything in my power to maximize my profits.

I understand that Dr. Malone was equally candid yesterday in his appearance here before the committee. The problem in that statement, though, is that John Malone's interests are not necessarily synonymous with the public interests.

And I again turn this right back to you as the Chairman of this panel and your colleagues on this committee and say please do something. Put your foot on the accelerator, and the reason being, cable's strategy is clear. It is very clear to me, that they are buying time, and the more time they can buy, the more product they can lock up, the more product they lock up, the more control they have and they don't care who gets into business. All the competition will have to buy from them. And I really believe that unless this body, this Committee, this Congress, this FCC—and I was very pleased to hear the testimony of Chairman Sikes—accelerates the process, cable will continue to gobble up without any restraint all of the program elements that encompass the business.

And again, I think we will have second class citizens in rural America.

And I believe wireless has something to offer. And let me tell you what we are. Wireless is an interesting product. The FCC created us in 1983 to create a competitive source against cable's distribution. From 1983 until now, it has been a desert. There has been very little done. We now serve 350,000 subscribers in 45 communities. We are making progress in spite of the impediments, in spite of the barriers to entry that cable has put in front of us.

I was pleased again to see Mr. Malone say he has competition from wireless cable. Well, that competition as a mathematical number says we are competing in .006 percent of the markets in the country. We think we have a very viable product, 33 channels of programming. You can pick a la carte. You don't have to go through eight tiers to buy our product.

Our technology works well. Again, cable suggested in some previous hearings that our technology was inferior.

We will compete and we will develop programming. We will do many things, but again you have to be in business to do that.

One of the things we are going to do that I think is very important to this country is we have a natural partnership with education. Twenty of the channels that we will provide are leased from educational organizations. According to the rules of the FCC, those channels will be programmed 20 hours each per week with education. We are going to deliver education into the home. We are going to do things for rural America that cable and others have not been able to do.

In my visit to South Dakota 10 days ago, I saw schools that today cannot afford science teachers. Therefore, the students in those high schools are not qualified to go on to university unless they go and get a qualification in summer school or from some other school. We will put education, we will put science into that school. We will put those courses into homes.

So, wireless cable really has a value to bring to the communities of this country, and we are looking forward for the opportunity.

Thank you very much.

[The statement follows:]

STATEMENT OF ROBERT L. SCHMIDT, PRESIDENT, WIRELESS CABLE ASSOCIATION

Mr. Chairman and Members of the Subcommittee, on behalf of the Wireless Cable Association, I thank you for the opportunity to participate in these important hearings on "Oversight of the 1984 Cable Telecommunications Act."

In my testimony I hope to accomplish three objectives:

o First, report to you on the improving state of the Wireless Cable industry and to explain why Wireless Cable is a "here and now" alternative to Big Cable that, if permitted to compete, can offer consumers a choice in communities throughout the country.

o Second, examine why the troubling anti-competitive trends which were examined by the Subcommittee most recently in June during its hearings on "Media Ownership" have continued to accelerate. Without your help now, Wireless Cable and others may never be able to fully meet their potential for providing television service to consumers.

o Third, comment on various legislative approaches which could remove the obstacles that currently block competition in the marketplace, including several of the bills which have been introduced by Members of this Subcommittee.

TIMELINESS OF HEARINGS ON 1984 ACT

The rationale that supported the major overhaul of telecommunications policy embodied in the 1984 Act, which in some important respects may have been dubious even then, is utterly inconsistent with the reality of today's marketplace. The 1984 Amendments were intended to "allow cable television to become a vigorous and effective competitor,"[1/] while at the same time serving "the best interests of consumers."[2/] Neither objective has been met: cable TV is not a competitor. It has grown into an industry dominated by a handful of powerful multi-system operators ("MSOs") who don't tolerate any newcomers on their turf and indeed don't even compete among themselves. And consumers' interests have not been served by the monopoly rates charged by cable operators.

The time for Congress to act is now. The cable television business, with its spectacular success, growth and increasing dominance of the marketplace, has long outgrown the need for the protection Congress provided in the 1984 Act. If the Subcommittee would permit an observation, it is often

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1/ 130 Cong. Rec. E855 (daily ed. Mar. 7, 1984) (statement of Rep. Bliley).

2/ 130 Cong. Rec. H10435 (daily ed. Oct. 1, 1984) (statement of Rep. Wirth).

difficult for Congress to get ahead of the curve when it comes to reacting to fast changing developments on complicated issues of critical importance to the country. By the time Congress is even institutionally aware of a problem, and is finally able to respond, the result is often too little or, worse -- too much -- too late.

I would submit that this Subcommittee with its communications policy expertise and the record it has been developing this year, together with the detailed testimony taken by other panels such as the Senate Antitrust Subcommittee and several committees of the House of Representatives, is in a unique position to act at precisely the right time. This Subcommittee has the expertise, and it has the information, to respond in a way that preserves the tremendous gains made in the last decade for advancing the distribution throughout the nation of quality television programming to consumers, while at the same time assuring that consumers are not threatened by an unregulated monopoly -- the cable television industry. It can do that by advancing legislation now pending in Congress which would stimulate competition with Big Cable, and give consumers a choice among different distributors of satellite television programming.

Let's not quibble about the principal finding that this Subcommittee should be able to make. The cable television industry is in fact an unregulated monopoly. It generates upward of $20 billion a year in cash revenues. The largest multi-system operator, Tele-Communications, Inc. ("TCI"), alone brings in over $300 million in cash a month. Cable television services now are available to 73.9 million of the 90.4 million households with televisions. Over 56 percent (56%) of the households with televisions subscribe to cable television.

Who regulates this behemoth? Since the 1984 Act took effect the answer is - No One.[3/]

[3/] The New Republic made the point as follows:

> Cable franchises are peculiar businesses that have slipped through the cracks separating our regulatory and antitrust agencies. Almost all communities with cable are supplied by only one franchise, for the same reason communities are supplied by only one electrical company; having two sets of cables running side by side through a town would be hugely inefficient. But whereas electrical utilities are regulated to prevent them from abusing their monopolies, cable franchises aren't: the Cable Act of 1984 took local governments' power to regulate them. Meanwhile, the FCC doesn't regulate cable either; it has deemed it a competitive industry, which requires only antitrust oversight. But the Justice Department, source of that oversight, looks upon each cable franchise as a natural monopoly subject to regulation, which must come from the FCC -- which won't do it -- or the municipality -- which can't. Guess who's benefitted from these interagency word games? And guess who hasn't? In the 12 months ending in October 1988, cable prices rose 13.6 percent, compared with 4.2 percent for the Consumer Price Index. And you can decide for yourself how diverse and innovative the programming is.

James Bennett, "Time Out," The New Republic, Apr. 24, 1988, p. 23.

The extent of the FCC's regulation under the 1984 Act has been to adopt a rule, the so-called "effective competition standard," which is just nonsense. This standard exempts from rate regulation any cable system which is located in an area where viewers can receive three somewhat fuzzy over-the-air broadcast signals. Under this standard 97 percent (97%) of all cable franchises are unregulated.

On all other questions relating to competition and antitrust compliance the FCC has deferred to the United States Justice Department. But the Justice Department, while recently making some rumblings about greater antitrust vigilance, has been virtually asleep at the switch while big trains like the Time-Warner merger roar through departmental review unimpeded.

Local government is no longer able to regulate the spiraling rates, poor service, or programming changes imposed on cable subscribers. As a check on the unregulated local monopoly, competition within franchise areas is nil. In any given community, if consumers are lucky enough to get cable at all, they usually can only get it from one company. Over 8,000 communities have been wired for cable, and in less than one percent (1%) of those communities do consumers have a choice of cable companies. In effect the message cable gives the local consumer is "if you don't like it, tough."

And there are many areas of the country which will never be wired by coaxial cable. Unless Wireless Cable and other alternatives to cable television -- which are willing right now to serve these largely rural communities -- are able to overcome obstacles that have been thrown in their way, people living in these areas of the country will in effect continue to be second-class citizens with respect to their ability to view television programming.

Not surprisingly, the American people are beginning to feel all the classic symptoms of an unregulated monopoly -- higher prices, poor service, restriction of product. The central issue before the Subcommittee at this time, in light of the voluminous record that Congress has been developing over the last two or more years, and in the face of the real world experience of your constituents, is "what are you going to do now for the American people about the cable monopoly?"

If you agree that the system created by the 1984 Act needs to be adjusted then your options are clear:

You can re-regulate.

Or you can intervene in the market structure, break-up the giants and divest their control over programming.

Or you can foster competition.

We believe that the preferable course is for Congress to assure that consumers have a choice by enabling alternative distributors of television programming to compete vigorously and fairly for the American consumers' business. I believe that our position is consistent with the views of the Administration recently expressed before this Subcommittee by the NTIA.[4] Judging from several bills already introduced, it appears that many Members of this Subcommittee agree.

STATE OF THE INDUSTRY

Let me tell you how the Wireless Cable industry is faring.[5] Although we continue to face very serious obstacles, I can tell you that Wireless Cable is alive and growing. Wireless Cable operations are up and running in 45 different communities across the nation and we presently enjoy an excess of 350,000 paying subscribers. We should emphasize, however, not only what Wireless Cable has already accomplished, but its potential. In virtually every other area of the country it is feasible for

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4/ Testimony of Janice Obuchowski, Director, National Telecommunications and Information Administration, before the Senate Communications Subcommittee (Nov. 1, 1989).

5/ The Wireless Cable Association is a trade association of firms and individuals who are involved in packaging and retail distribution of satellite-delivered programming to the public through wireless cable systems. Simply stated, wireless cable is cable; except that over-the-air frequencies are used rather than coaxial cable lines to deliver program services to subscribers. Although design varies from operator to operator, the typical wireless cable system receives its satellite-delivered programming using earth stations located at the system headed. The wireless cable system then retransmits that programming in scrambled form to small roof top antenna systems via up to 33 video channels assigned and regulated by the FCC. At each subscriber's premises, the wireless cable programming and all locally available broadcast television signals are fed over coaxial cable to a set-top decoder/channel selector box, through which the subscriber can tune to any available channel.

Wireless Cable operations to give consumers a choice in satellite programming. This potential for growth was recently reaffirmed by Senator Slade Gorton (R-WA) who predicted, "With any kind of good luck, and reasonable business opportunity, hundreds if not thousands of systems, with millions of subscribers" will be operating in the future.[6/]

In September the Wireless Cable Association held its largest, most successful annual trade show ever with twice as many attendees and more than double the exhibition space over just the previous year. I am happy to report that there has been some progress in Wireless Cable operators gaining access to programming, as indicated by the attendance and exhibitions of major programmers at the recent trade show. The Discovery Channel and The Disney Channel, for example, have become generally available to Wireless Cable and I understand they are doing quite well with us. They find, as other programmers have, that Wireless Cable offers an individually addressable system

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[6/] Remarks of The Honorable Slade Gorton, Wireless Cable Association Trade Show, Crystal City, Virginia (Sept. 12, 1989). Others have been at least as optimistic about the potential. See Multichannel News, Sept. 11, 1989, p. 10 (quoting prediction of wireless service in 25 million homes within two to three years, by George Schulman, Vice President of Marketing for Starion Entertainment Network). See generally, Paul Kagan Associates, Inc. "Wireless Cable Report", Multicast.

which is even less susceptible to piracy then is a conventional coaxial cable system.[7]

Wireless Cable systems also are less capital intensive than coaxial systems and have cost efficiencies which necessarily mean, when they are able to compete head to head, that Wireless Cable is able to offer consumers competitive prices for comparable programming.

Wireless Cable is continuing to fulfill the role envisioned for it when it was created by the FCC, making a major contribution in the field of education.[8] The FCC, in permitting Instructional Television Fixed Service ("ITFS") spectrum to be made available to Wireless Cable, made educational programming an integral part of our business. Up to 20 ITFS channels may be leased from educational institutions to Wireless Cable operators, but an ITFS channel is only available for commercial use if it is used for a minimum of 20 hours a week for educational programming. Through this use of ITFS channels an expansion of Wireless Cable systems results in an expansion of educational services available to communities -- up to 400 hours per week --

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[7] For example, Cleveland's MetroTen wireless cable operations uses the Zenith Z-TAC security system, a system which is superior to that used by many of the cable systems currently carrying HBO and other satellite television programming. Indeed, the trade press reported recently that HBO insisted that the New York wireless cable operator employ the Z-TAC system. I can't think of a more eloquent testimonial to the security of our system.

[8] 47 C.F.R. § 74.931(e).

and a direct financial benefit to educational institutions which receive license fees for otherwise unused channel capacity.

In sum, at the present time Wireless Cable represents an established technology capable of competing with the coaxial cable industry in the delivery of multiple channels of video programming on a widely available basis.

Despite this healthy and promising prognosis, Wireless Cable is still frustrated from reaching its full potential for a very simple reason: Big Cable has an ever tightening grip on the programming we need to serve consumers. Unfortunately, Wireless Cable still is generally unable to obtain what I call the four crown jewels of satellite television programming -- HBO, Showtime, TNT and ESPN. Wireless Cable also has serious difficulties in obtaining rights to transmit regional sports network pay programming.[9] Without the ability to offer these most desired programs to consumers, many Wireless Cable systems are unable to get the financial backing necessary to become operational.[10] Those systems that are operational, and it could

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[9] Statement of William K. Hoffman, Vice President and General Counsel, The Microband Companies, Inc., submitted to The Subcommittee on Antitrust of The United States Senate Judiciary Committee on The Subject of The Availability of Sports Programming (Nov. 14, 1989) (attached).

[10] Investment analysts state that cable industry consolidation is the main factor discouraging cable overbuilds and other forms of competition. See, e.g., Communications Daily, Oct. 23, 1989, at 6. This issue was also raised in Senator Metzenbaum's letter to James Rill, Assistant Attorney

(continued...)

be a much larger group, experience severe disadvantages both in competing head to head with cable and in serving unwired areas because they have difficulty in assembling a competitive package of programming to offer consumers.

The systems which have been able to acquire rights to any of the crown jewels have done so either through litigation, or because they acquired grandfathered contract rights from the previous single channel distributor, or in some instances by acquiring a cable franchise. And even when such programming is acquired, it often is available only under severely discriminatory terms and conditions. As I'm sure the testimony of our colleagues from the rural cooperatives and the backyard dish ("TVRO") industry will be able to document, the prices that we are forced to pay for programming are often several multiples higher than those paid by local cable operators for the same programming. In addition we often experience "red-lining"; that is, the Wireless Cable operator is restricted from carrying programming in areas where there is already a cable operator.

We are not alone. You will hear the same story from anyone else who tries to get into business and compete with Big Cable. There is always an excuse or a rationale to disguise what

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10/(...continued)
General, expressing concern over TCI's acquisition of Showtime (Oct. 19, 1989). See also "Ops See Wireless 'Window of Opportunity'", Multichannel News, Sept. 18, 1989, p. 53 (discussing difficulties of obtaining financing).

is really happening -- that programmers are coerced by their Big Cable partners and not permitted to sell to alternative distributors. The Subcommittee will hear the same story from representatives of the TVRO industry, from rural cooperatives, from the satellite master antenna television ("SMATV") or private cable operators, and even from small independent cable operators. Most recently, Big Cable has mounted an all out campaign to keep telephone companies out of the cable business. The common factor in all of these cases is that every time somebody knocks on the door and tries to get into the marketplace and offer consumers a choice, cable will do everything in its power, which is quite enormous right now, to keep competitors out and maintain its monopoly.

Programming is not available to Wireless Cable because of the enormous market power of the few large MSOs which run the market and because of vertical integration between cable MSOs and cable programmers whereby the operators and programmers increasingly have common ownership. Because of the horizontal market power of the cable industry a programmer, even an "independent" programmer, will succeed or fail only at the pleasure of the industry. Moreover as a result of vertical integration, cable programmers have the incentive and the ability to favor their affiliated cable system operators over other distributors of video programming.

Over the last three years no programmer has launched a new service without cable taking a significant equity position in that programming. Since your last hearing, both HBO and Showtime have sought cable equity for their soon-to-be launched comedy channels, and TCI, the largest MSO, has announced its intent to acquire fifty percent (50%) of Showtime.

Just this week there have been reports that TCI, perhaps in partnership with Turner Broadcasting, will make a bid for MGM/United Artists.[11/] Frankly, I was afraid to let the ink dry on this testimony for fear I would miss including another major acquisition.

HBO has never in its history yielded equity to cable MSOs. HBO originally had intended not to offer an equity position to cable; then in the weeks immediately proceeding the launch it apparently realized that in order to succeed, it would have to allow cable MSOs to buy into the service in order to obtain the degree of system penetration sufficient for the venture to survive.[12/]

Similarly, Showtime has reportedly offered operators a fifty percent (50%) stake in its new comedy channel, HA! The

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11/ Laura Landro, "MGM/UA Bid Being Planned by Cable Group", The Wall Street Journal, Nov. 14, 1989, p. A2.

12/ "HBO Said to Discuss Sale of Comedy Channel Stakes," The Wall Street Journal, Nov. 6, 1989, page B6.

Comedy Network.[13] Showtime, like HBO, apparently recognizes, and respects, the leverage that the MSOs have over programming services. Just a few days ago we read reports that Showtime and HBO, which historically have been adversaries in all aspects of the cable business, may be forced by the cable MSOs to abandon their plans to have two separate comedy channels, and instead agree to a jointly owned comedy channel.[14]

This leverage was also demonstrated recently in TCI's plan to buy a fifty percent (50%) interest in Showtime. TCI already owns an interest in at least 12 other programmers.[15] One wonders whether the troubled Showtime had much of a choice, whether TCI made an offer it couldn't refuse. In fact, there are reports that TCI is also negotiating TCI's carriage of MTV, VH-1, and Nickelodeon which are owned by Showtime's parent Viacom. I would suggest that the Subcommitteee explore whether the TCI-Showtime deal also includes an arrangement involving these other

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13/ "Comedy Channel Offering Equity Interest to MSOs", Multichannel News, Nov. 6, 1989, p. 1.

14/ Wall Street Journal, Nov. 14, 1989, p. B6. The article also reported that Time Warner and Viacom have been under pressure to settle their antitrust litigation, "particularly now that the cable industry is coming under increasing scrutiny in Washington, D.C." Id.

15/ "TCI investments include 50% of American Movie Classics, 14.3% of Black Entertainment TV, 36.4% of Discovery Channel, 43.6% of Fashion Channel, 60% of Home Sports Entertainment, 80% of Netlink, 35% of Prime Time Tonight, 60% of Rocky Mountain Prime Sports Network, 37.5% of Think Entertainment, 11.5% of Turner Bcstg., small holdings in 2 shopping channels." Communications Daily, Oct. 19, 1989, p. 5.

affiliated services.[16] TCI executives explained that this most recent acquisition was needed to assure continued access to programming as well as to compete with Time Warner.[17] Recall that Time Warner argued that it needed to be big to compete with foreign companies. These are very convenient rationalizations for market dominance.

Facing this kind of power, a programmer cannot afford to displease the large MSO's by giving a newcomer like Wireless Cable a small toehold and allowing it to sell its product, even in areas where there is no coaxial cable system. Ordinarily one would expect a programmer to maximize the number of subscribers who view its programming, and to sell its product to as many outlets as possible. If programmers are acting inconsistently with this basic economic principle other, anticompetitive forces must be at work. By withholding its product from a distributor such as Wireless Cable that is willing to distribute in unwired areas, assuming the distributor meets reasonable financial and other business criteria, a programmer is not acting in its own economic interest but rather in the anticompetitive interest of Big Cable.

16/ "TCI Buys Into Showtime", Satellite Business News, Nov. 1, 1989, p.26.

17/ "TCI's Showtime Stake Puts A New Face On Many Cable Relationships," CableVision, Nov. 6, 1989, p. 11.

Again, we need your help now. Self help thorough private antitrust litigation is an imperfect and sometimes, under current law, an uncertain remedy for us. At best it is extremely costly and time consuming. On a case-by-case basis, when adequately funded operators have pursued this route, they have succeeded.[18] But for an entire industry to rise or fall on private legal actions is not much of an answer -- especially when there is such an immediate demand for increased competition in the marketplace, as the FCC originally envisioned back in the mid 1980's when it first created the Wireless Cable multichannel service.[19]

18/ A telling exception occurred in Chicago, Illinois when People's Choice TV announced plans to expand from its single channel to a multichannel service, capable of competing with cable. Viacom refused to provide Showtime/The Movie Channel any longer to People's Choice TV. When People's Choice TV sued, Viacom retaliated by refusing to allow People's Choice to serve as many as 100,000 new SMATV customers in Chicago, Dallas, Minneapolis and Houston.

See Testimony of Robert L. Schmidt, President of the Wireless Cable Association, before the Subcommittee on Telecommunications and Finance, House Committee on Energy and Commerce (June 15, 1988).

19/ In 1983, when the Federal Communications Commission amended its rules to make wireless cable possible for the first time, the Commission recognized that "there is no multichannel alternative to cable available now." Amendment of Parts 2, 21, 74 and 94 of the Commission's Rules and Regulations in regard to the Instructional Television Fixed Service, the Multipoint Distribution Serve and the Private Operational Fixed Microwave Service, 94 F.C.C.2d 1203 (1983), reconsideration denied, 49 Fed. Reg. 27,147 (July 2, 1984).

Already, the close scrutiny that Congress has given to the denial of access to programming issue has brought some relief and some improvement in our situation. But we are a long way from realizing our full potential in the marketplace as are others who are similarly situated. We therefore must come to the conclusion that legislation is essential. The market imbalance unintentionally caused by the 1984 Act needs to be corrected.

THE NEED TO REVISIT THE 1984 ACT

When Congress passed the 1984 Act it was generally believed that cable needed a helping hand. Cable argued that it needed to get out from under the thumb of cities who, in effect, were asking for too much. Moreover, in order to vie for the right to distribute programming in lucrative markets, many cable operators were "gold plating" their systems, offering promises and benefits in an effort to win a franchise which ultimately would prove very costly if not impossible to fulfill. The argument that apparently prevailed in Congress was that regulation by the cities was unnecessary because cable would face stiff competition from DBS, Wireless Cable ("MMDS") and other quarters, and that in any event cable would always be held in check by competition from the broadcast television industry.

Since 1984 the cable industry has been able to accomplish more than any one might have dared to expect. Cable in effect has rewritten some of the viewing habits of the television public so that new program services have been able to provide market niches that simply didn't exist before. Cable has also created a monopoly of "basic cable" which in virtually every community cable can only be purchased from one provider. There is no second provider.

Cable television currently is a multi-billion dollar a year cash business that is growing at the rate of 10 percent (10%) a year. When Congress considered the 1984 Act, cable systems were valued at $1,000 per subscriber. Today franchises are sold at a price of $3,000 per subscriber and more. In 1984, there were still very few conventional banking institutions willing to invest in cable television. Since 1984 cable has become the darling of Wall Street and is touted in investment brochures as a monopoly business.

Thus the 1984 Act has condoned, and in some ways promoted, an environment in which competition cannot develop. The chief reason that competition cannot develop is because other potential distributors of video programming do not have access to the programming they need to serve consumers. Simply put, in 1984 Congress did not focus on the availability of programming to alternative providers because the alternative technologies were not in business yet and problems of access had not yet materialized.

Big Cable has become such a vested interest, so intent on maintaining its position on top of the hill, that its philosophy has changed from "let us compete" to "let us maintain the status quo, trust us, the public will be better off."

In response I would like to state three reasons why legislation is needed to promote competition to Big Cable.

First, Big Cable, despite its success and growth, does not intend to, and will never, serve a substantial portion of America -- especially rural communities.

Even when product is available in rural communities it often will be sold at extremely high prices relative to the prices that subscribers pay in suburban and urban areas. Rural America will also be denied the important educational benefits now available through television programming. The Members of the Subcommittee know all too well that in rural America we have, in some areas, only a second class education available for our children. In many places, for example, I understand that there are more schools than there are science teachers. Television technology, indeed Wireless Cable technology and other means of distribution, can offer needed courses in schools and in homes, along with news and entertainment programming. But these distribution systems, those alternatives to Big Cable which are willing to provide programing throughout America, including rural communities, are blocked from even doing business in areas where the coaxial cable industry never intends to go. This is because it is in Big Cable's interest to prevent others from establishing any beachhead in the business.

I challenge any of the witnesses from the cable industry who have appeared before this Subcommittee to offer one single legitimate business reason why Wireless Cable, or private cable, or a rural cooperative should be prevented from transmitting HBO, TNT, ESPN or any other programming into communities where no Big Cable company is ready or willing to provide service. I submit that if programmers were free and independent of the influence of Big Cable, it would be in their interest to serve an important part of our population that is not currently served by any multichannel provider.

Second, cable achieved its position of dominance with a big helping hand from Congress in the form of first, the compulsory license, and second, the 1984 Act's rate deregulation. Big Cable is accelerating its consolidation of power and exercising even more control over programming in order to assure that other distributors are unable to follow in its footsteps and succeed in the marketplace.

Cable often attempts to justify its monopoly status by claiming that it took a risk and created the programming which is now being denied to Wireless Cable among others. Wireless Cable and other potential new entrants into the marketplace, Big Cable asserts, should take their own risks and create their own programming.

However, the cable industry's collective memory is evidently very short. I, for one, remember the "good old days" of the early to mid-seventies, and cable's battle with broadcasters over the compulsory license. At that time, it was cable that argued that access to programming at reasonable rates was necessary to enable the fledgling industry to compete. Cable prevailed in its argument and was granted a compulsory license which allowed it to carry certain broadcast programming for a very low rate. It was this advantage more than anything else that enabled cable to quickly consolidate its position in local markets and reap substantial profits. And these monopoly profits have in turn enabled the cable industry to buy existing programming services. Time Warner and TCI's acquisition of a half-interest in Showtime are but the most recent examples of this phenomenon.

This is not risk-taking. Cable would not be in the position it enjoys today had it not been for the benefits it received early on from its compulsory license. Neither Wireless Cable, nor any other potential alternative distributor, could today create its own programming in any realistic way.

Television transmission technologies are, in a very real sense, creatures of FCC regulation. We all, cable included, owe our existence in some part to FCC rules. The first of the FCC decisions that made Wireless Cable possible as a commercial venture was not issued until late 1983 and it took several more years for the complete regulatory structure to be put in place.

By this time, cable -- whose regulatory fate had been decided much earlier -- had enjoyed nearly two decades of unparalleled growth, thanks in part to the compulsory license I just mentioned. During this period when cable faced little or no competition in the local market because alternative commercial distributions systems such as wireless were not legally possible, the industry was able to use its monopoly profits to enter into exclusive arrangements for programming.

As a result we face, a situation today where, for example, there is only one major movie studio -- MCA/Universal -- that does not have an exclusive arrangement with a premium programming service. Time Warner's HBO has exclusive deals with Cannon, Columbia/TriStar, Lorimar, MGM/UA, New World, Paramount, Twentieth Century Fox, and Warner Bros. Showtime has entered into exclusive arrangements with Disney/Touchstone and Orion, and has announced a major distribution deal with Columbia Pictures and Tri-Star. Given HBO's and Showtime's locks on these studios' best product, it is disingenuous at best for Big Cable to assert that Wireless Cable should launch its own movie channel. By a fortuitous set of regulatory circumstances, cable got a jump on competing technologies and was able to corner the market for movie product. For cable now to claim that the same opportunity is available to Wireless Cable and other competing technologies simply ignores the realities of the marketplace.

Third, Big Cable will not voluntarily clean up its act. Its commitment to price restraint, customer service, and meeting its obligations to the community and to education will only improve if there is more competition.

You probably have heard about the cable industry's calls for price restraint at its most recent annual show. It is a fact that this warning is in direct response to Congressional scrutiny, the still distant prospect of competition, and perhaps some fear of telco entry into the business. Still, it is clear that big rate increases are the norm in many communities, including those served by some of the very people who have cautioned the industry to moderate prices. For example, in October, Mile Hi Cablevision announced that its 69,000 subscribers in Denver would face their second rate increase in ten months amounting to a nineteen percent (19%) hike.[20/] Mile Hi also increased its premium rates. Closer to home, in Fairfax County, Virginia, Media General just announced a fifteen percent (15%) increase in monthly basic rates from $19 to $22.[21/] Big Cable has tried to make the huge rate increases by the Multivision West Tennessee system, which has received so much

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20/ Thomas P. Southwick. "A Gift for Cable Foes," Cable World, Oct. 9, 1989. Nationwide, cable rates rose 0.8 percent in September, almost triple the 0.3 percent increase for all consumer items monitored by the CPI that month. Multichannel News, Oct. 23, 1989, p.3.

21/ John M. Higgins, "Rate Hike Comes Home to Roost in D.C.", Multichannel News, Oct. 9, 1989, p. 32.

attention from Senator Gore, look like an isolated incident involving an industry rogue. The facts just don't fit this fantasy.

The truth is that deregulation of rates won't work without competition. With competition, the consumer is always better off. Ironically, there is the point recently made by TCI Chairman John Malone in a slightly different context, in order to defend the shift of sports programming from broadcast to cable. He said:

> Wherever we have gone, the entrenched industry has always claimed reduced benefits to the consumer. What really happened is that we put pressure on the entrenched business to compete. The result has been more sports on over-the-air TV, not less. I don't think we'll put broadcasters out of business. But we may make them get a little better at what they do, make them adjust and maybe pay a little more for sports events because there is more competition.[22]

Because of the mere prospect that Congress might act to re-regulate or provide some competition, cable has become concerned about improving its image. Recently launched programs by some of the large MSOs to assist education and provide community service are commendable to say the least. But just think how much of a contribution that Big Cable would make in these areas if they were challenged by real competition.

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[22] Quoted in Communications Daily, Nov. 8, 1989, p. 4.

WIRELESS CABLE SUPPORTS LEGISLATION DESIGNED TO PROVIDE FAIR ACCESS TO PROGRAMMING AND PROPOSES COMPULSORY LICENSE AMENDMENTS

From our perspective the most important cable oversight issue for the Subcommittee is how to eliminate the discriminatory practices which prevent Wireless Cable or any other alternative distributor from obtaining the programming needed to serve consumers. Many bills have already been introduced in the Senate which address this problem in slightly different ways, including:

S. 168 - Cable Television Programming Competition and Consumer Protection Act of 1989

> This bill prohibits price discrimination and exclusive distributorships for satellite-delivered programming, and was introduced by Senator Larry Pressler on Jan. 25, 1989. With this bill, Senator Pressler fulfilled a pledge to the wireless cable industry that he made at its 1988 trade show in Crystal City. The bill was referred to the Senate Commerce Committee.

S. 833 - Cable Television Subscriber Protection Act of 1989

> This bill redefines the term "effective competition" under the 1984 Cable Act to allow regulation of rates of basic cable service unless the cable community is served by more than one multichannel (non-broadcast) video programming distributor. It exempts from rate

regulation cable systems that have less than 30% penetration in their franchise areas. This bill was introduced by Senators Metzenbaum and Lieberman on Apr. 18, 1989, after Senator Metzenbaum chaired his second hearing in a year in which his Antitrust Subcommittee examined anticompetitive practices of the cable industry. S. 833 was referred to the Senate Commerce Committee.

S. 834 - Competition in Cable Television Act of 1989

This bill prohibits unreasonable discrimination in the sale of programming distributors, and prohibits any one cable company from owning systems that serve more than 25% of the cable subscribers in the country. This bill, which contains the fair access to programming provisions long sought by wireless cable, was introduced by Senators Metzenbaum, Pressler and Lieberman on Apr. 18, 1989. It was referred to the Senate Judiciary Committee where it is awaiting action.

S. 905 - Cable Consumer Protection Act of 1989

This bill amends Section 623 of the Cable Act to allow regulation of cable rates and permit states or franchising authorities to regulate cable service. The proposal also authorizes a state to deny a cable franchise renewal or transfer of ownership or control of a cable system on the grounds of extensive media ownership, and conditions compulsory licenses upon carriage of local broadcast signals. The bill was introduced by Senator Lieberman on May 3, 1989 and was referred to the Senate Commerce Committee. A companion measure, H.R. 2222, was introduced in the House by Representative Christopher Shays (R-CT) and was referred to the Energy and Commerce, and Judiciary Committees of the House.

S. 1068 - Cable Competition Act

This bill represents Senator Al Gore's effort to offer a comprehensive multi-title legislative solution to the problems he sees facing the television consumer. The bill would allow franchising authorities in areas without competition to regulate rates for the so-called "life line" service, defined as the lowest priced tier, which includes local broadcast signals. It would also allow telephone companies to provide cable services

> inside and outside their service areas. The bill further requires cable operators, including common carriers, to provide access to the system for all programming services unless this is not feasible because of the limitations of channel capacity or because the nature of the program and content does not comport with local standards. Like Senator Metzenbaum's proposal, this bill contains provisions sought by the wireless cable industry and others to assure that programming services affiliated with cable operators are available to all program distributors on a non-discriminatory basis. Finally, the bill mandates an investigation by the Federal Trade Commission into concentration within the cable programming industry. Joining Senator Al Gore as original co-sponsors were Senators Slade Gorton (R-WA) and Wendell Ford (D-KY). A companion bill, H.R. 2437, was introduced in the House by Representative Rick Boucher (D-VA) and co-sponsored by 14 of his colleagues.

And just this past week, Senator Danforth introduced "The Cable Television Consumer Protection Act of 1989." Among other things it allows cities to regulate rates unless the cable system faces competition from another multichannel provider such as wireless cable. It bars cable programmers affiliated with cable operators from discriminating against non-affiliates in the price, terms, conditions or availability of its programming. It also caps the size of MSOs to fifteen percent (15%) of cable subscribers.

We embrace these bills and welcome their intent and pledge our willingness to work with the Subcommittee to move the effort forward. One aspect of these various proposals that we especially hope to address is the need to focus on the availability, not only of programmers directly owned or controlled by Big Cable, but also those which are not. The power of the larger MSOs is such that they can coerce programmers owned by other MSOs, as well as so-called "independent" MSOs. In considering legislation we urge the Subcommittee to bear this phenomenon in mind.

In addition, Congress should:

- Create a compulsory license for alternative distributors, similar to that which coaxial cable enjoys. We urge Congress to grant Wireless Cable and other fledgling technologies in the 1990s the same sort of boost it provided to cable in the 1970s, namely, guaranteed access to the programming needed to compete in a meaningful way in today's market -- just as the compulsory license aided cable during its infancy.
- Examine whether Big Cable (MSOs of a certain substantial size) still needs to be propped up by a compulsory license. Just as we would suggest a sunset on any compulsory license that would be granted Wireless Cable, isn't it time to let Big Cable compete on its own two feet?
- Be prepared to order Big Cable to divest control over programming if competition does not emerge. There are ample precedents -- CBS was required to get out of the cable business, networks have been blocked from production through the Finsyn rules, and the movie industry has long been prohibited from controlling movie theater outlets.

Whatever the ultimate remedy, Congress should act now to eliminate the anticompetitive forces at work in the marketplace.

Senator GORE. Thank you very much, Mr. Schmidt.

Let me ask a few questions to each of you.

Mr. Phillips, I understand that the Disney channel has generally been the most TVRO friendly programmer in its dealings with NRTC. Is that correct?

Mr. PHILLIPS. Yes, I think that is correct. We have had a very good relationship with them since entering our contract, and it has been growing very well.

Senator GORE. Would it follow that Disney's willingness to be friendly and cooperative with NRTC might be based on the fact that it is practically the only premium service totally independent of cable ownership?

Mr. PHILLIPS. I certainly think from my experience that has a lot to do with it. We have talked with them about philosophy, and we noted the way they look at this market and the potential here. And it is somewhat different from the other programmers that are intertwined with cable.

Senator GORE. I do not mean this question to be humorous. I really am looking for objective evidence. Do you sense a hostility on the part of the programmers to satellite dish owners?

Mr. PHILLIPS. I don't think it is so much hostility as it is opportunism, as I said in my remarks. I think Mr. Mooney was correct yesterday when he said that some of the programmers see an opportunity here to go direct to the customer and compete directly at retail.

The problem with that is that by doing that, they have exercised their competitive advantage of keeping control of the product for themselves, and by doing that, they have been able to go direct and charge many, many more times what they charge a cable operator for the same level of service.

That has been NRTC's concern. We want to be a competitor in that market. We want to, and do in fact, do everything that a cable company does. We can authorize subscribers, service them, bill them, advertise and market to them, but yet we are still forced to pay these extreme price differentials when compared to cable.

Senator GORE. Now, why do you think you are being forced to pay 441 percent more?

Mr. PHILLIPS. Well, the programmers that have agreed to sell to us and to some other sources have basically looked at the cable market as one price, and the home dish market is served at another price.

Senator GORE. Why?

Mr. PHILLIPS. Opportunity.

Senator GORE. But they are not cable companies. They are programmers.

Mr. PHILLIPS. Well, I guess you are suggesting here and I have suggested in my testimony that there is a natural reason for that. It creates a barrier for cable. It keeps the price of the dish service up so that it won't penetrate inside of any cable areas. It's not competitive.

Senator GORE. Do you think that is the main reason why they keep your wholesale prices so high?

Mr. PHILLIPS. I think that is the control that we see exerted from the intertwining of those programmers with the cable owners, and

I also think that is the opportunism that we see from inside of those programmer companies themselves.

Senator GORE. In other words, when the programmers negotiate with you and set the wholesale price that you pay in order to get the signal and turn around and sell it to your dish owners, when the programmers are negotiating that wholesale price with you, you think that one of the factors they have in their mind is the need to be sensitive to the price that cable customers are paying and the wholesale price that cable systems are paying. You sense that you want to keep the price you are paying higher than the price the cable companies are paying. Right?

Mr. PHILLIPS. I think in the discussions I have had with them, that is evident to me.

Senator GORE. Have they said as much?

Mr. PHILLIPS. I think they have indicated that cable is the source of delivery of choice.

Senator GORE. For them, for the programmers.

Mr. PHILLIPS. It's a strong competitor in that area, and it may not be effective to have a second competitor in there. It is confusing and it doesn't help the market. I have heard those kinds of comments.

I have had comments such—and there is a letter in the record from TNT that says our product is not available to you at any cost because it is a cable exclusive product, and we want it only available to cable in those areas where they serve from them. And we will serve the other areas ourselves and take care of those direct. So, it is essentially protection of cable as the provider of that exclusive product, TNT.

Senator GORE. Well, you think that somehow the cable industry has a degree of control over the thinking process these programmers go through when they deal with you.

Mr. PHILLIPS. I think that is true, and I think beyond that you heard testimony yesterday from Mr. Malone. He said we don't charge ourselves for delivery of TBS by Tempo. Now, in my book, Senator, there is a law that says that—section 202 of the Communication Act forbids satellite carriers from discriminating in the delivery of like services in communications. He told this subcommittee that Tempo sells or offers their service to TCI and doesn't charge anything.

I have testified to you that I pay 90 cents for that same product, and that's a fact. I think that that is against the law.

Senator GORE. So, he pays nothing. A small cable system pays 10 cents per customer per month. They force you to pay 90 cents per customer per month.

Mr. PHILLIPS. That's correct.

Senator GORE. Now, Mr. Mooney stated yesterday that the primary reason non-cable satellite dish programming distributors pay more at wholesale is that the cable companies provide more services to the programmers. Are you not able to provide full distribution service, that is, marketing, a computer system to turn on customers, a single payment each month to the programmer and so on? Can you provide those kinds of services?

Mr. PHILLIPS. Yes, Senator, we do provide those services. We have set our business operation up such that we come to the programmer and offer to take on all responsibilities, to authorize customers, market to customers, bill the customers, stand the credit and the payment responsibility to the programmer, and we offer them one check per month with no other responsibility on their part.

Senator GORE. Well, maybe they think you're not reliable, that you're a fly-by-night operation or something. You have a pretty substantial undertaking, don't you? You have a pretty well established financial base, don't you?

Mr. PHILLIPS. We are now paying programmers something in the neighborhood of a half a million dollars a month for programming, and we pay on time and honor our responsibilities. Yes, sir.

Senator GORE. Well, now, what you are telling me is that you provide to the programmer every service, every courtesy, every amenity, everything that a cable company distributor provides. Well, what is the reason why you have to pay higher wholesale prices than local cable companies for the same electronic signal? You are not causing the programmer to incur any additional costs, are you?

Mr. PHILLIPS. No, Senator, we do not. In order to engage in the home satellite dish business—Mr. Malone touched on this yesterday—a programmer must have a scrambler at their head end. He mentioned a fee of a half a million. And I checked that, and the actual fee from General Instrument for a fully redundant scrambler is $200,000. That is a one-time investment. That covers the scrambling of the signal for both the cable market head-ends and the home dish market. It is a dual use facility.

Secondly, you have to connect your head-end to the DBS authorization center that he mentioned. He quoted you a figure of $50,000 per month. I have a letter in my hand from General Instrument that quotes the new fees for those charges at $3,575 per month for a tier bit, which is the switch to turn the signal on for each descrambler, and a scrambler connection fee, which is actually just connecting to that California center, at $715 a month. So, for less than $5,000 a month, you can be involved in this business as a programmer.

From there if you sell to NRTC, you do nothing. NRTC has the capability. We have our own line into the DBS center. We can authorize service direct for the customer. We can turn the decoder on and off, and we will pay the bill direct to the programmer. There's nothing else the programmer has to do.

Senator GORE. So, the programmer doesn't incur any additional costs?

Mr. PHILLIPS. The only costs to serve the home dish market are the ones I just described that I know of.

Senator GORE. Very minimal costs. If you amortized that over the number of customers you have, how much per customer per month would that come out to?

Mr. PHILLIPS. We have looked at it and it would range between 2 cents and 5 cents at the very most.

Senator GORE. All right. Well, now, I still don't understand then. Mr. Malone is getting TBS for nothing. Some are paying 2 cents per customer per month. A small cable system pays 10 cents per customer per month. I still don't understand why you have to pay 90 cents per customer per month.

Mr. **Phillips**. The only thing I can tell you is that we have been debating this issue at the FCC. There is an ongoing investigation that Chairman Sikes mentioned.

Senator **Gore**. Yes.

Mr. **Phillips**. And the position that the carriers, in this case the satellite carrier is Tempo, and their lawyers have taken is that it is all right to charge a rate of 90 cents or whatever it is to the home dish distributors as long as it is a nondiscriminatory rate among the home satellite dish distributors.

Senator **Gore**. But there is only one.

Mr. **Phillips**. Well, they also have a rate card if you are a dealer.

Senator **Gore**. Okay.

Mr. **Phillips**. If they do the authorization for the dealer and other services that NRTC performs for itself, the dealer pays more than 90 cents.

Senator **Gore**. So, it is all right to discriminate against all satellite dish distributors.

Mr. **Phillips**. Equally, yes.

Senator **Gore**. Well, let me just pin this down. What you have testified here demonstrates that there is no economic reason for the discriminatory charge. There is no apparent justification due to cost incurred by the programmer for the extremely large markups you are required to pay.

You have also testified that after much experience in negotiating with the programmers, your belief is that somehow the cable industry has a powerful effect on the thinking process they go through when they deal with you, and that their motivation is to prevent new competition from a new technology of a kind that might complicate or discomfort the cable television industry.

Is that a fair summary?

Mr. **Phillips**. I think that is fair. The only thing I would add is that I think the programmer is willing to allow the dish market to grow as long as they make a very opportunistic margin and as long as cable has some protection.

Senator **Gore**. But free and untrammeled competition is something that horrifies the cable television industry.

Mr. **Phillips**. I think so, and the reason I can say that is because it made sense to us from the beginning in the dish market that if programmers would have charged fair rates, rates that customers that have dishes could afford, there would be no economic justification to pirate that signal and to break the decoder technology.

Senator **Gore**. Right. Well, we have come down as hard as we know how to on the piraters and on the people who are trying to sell these illegal descramblers.

But, you know, there is a lot to what you say and what Mr. Dawson says, that the flip side of this coin is if you put up a Berlin Wall around the programming signal, people are going to try to get over that wall. And they are going to take out hammers and chisels and try to punch holes in that wall.

These are issues that are related. And the way to stop the program theft is to have the criminal penalties, yes, but at the same time pay attention to the structure of the marketplace that allows this obscene monopolistic control.

I think your testimony, low keyed as it is, Mr. Phillips, is absolutely devastating to the cable industry's assertion that they are not involved in something wrong here. What they are doing is wrong.

Now, Mr. Dawson, let me ask you the question I began with in my colloquy with Mr. Phillips. Do you feel there is an intent by the programmers to stifle the development of the home satellite dish industry and market?

Mr. DAWSON. Sir, I not only feel there is an intent. I feel like I have in front of me everything it takes to prove it.

You know, the gentleman next to me, Bob Schmidt, was touting wireless cable, and it is certainly a wonderful, new alternative. But a satellite dish does have all the signals already, and we can't even get the cable owned programmers to acknowledge that we can get the signals. They would rather brainwash the public through lies and distortions and state that TNT, the channel which wireless cannot get which you can get on any satellite dish—they would rather state that it is exclusively on cable—that it is exclusively on cable. That's an overt lie.

The hit ads that used to come out on satellite—satellite is such a powerful technology, such a wonderful technology for the average citizen, it sends chills up the cable programmer and cable operator's back to think that such a technology might be loose and not under their control. So, what they would like to do is brainwash the consuming public into thinking that everything is only available on cable. They are the purveyors and the owners and the controllers of everything.

They did this early in the game to satellite dish. When Steve Efros of CATA came out with an organized program—he was quoted last month in Multichannel—I believe it was last month—as saying this was one of the most successful programs he ran, and they ought to run one like this right now on the telco entry situation to solve the problem.

Well, this is the ad that they ran back in 1985. It said, "Don't be fooled." It has the international signal crossing out a satellite dish and telling consumers that there is no way a satellite dish would ever pick up anything. As a matter of fact, you can turn it over and make a birdbath out of it. Here is a satellite dish sinking a whole house and property and apartment complex, and the people in it saying buying a home satellite dish is more costly than you think. These are hit ads.

Senator GORE. Now, wait a minute. Let me see if I can understand the significance of what you are saying. You are saying that the cable television industry is running advertisements and sending messages in their bills to their customers with the message that satellite dishes are a poor investment and that people should not consider buying a satellite dish. Correct?

Mr. DAWSON. Absolutely correct. Orchestrated campaign. If I could go on further, I can show you these are some of the orchestrated campaigns.

Senator GORE. Well, it seems to me that that does serve as evidence that the cable television industry identifies the satellite dish industry as a direct competitor.

Mr. DAWSON. Absolutely, absolutely.

Senator GORE. And they are running the ads in order to persuade people to choose cable instead of a satellite dish.

Mr. DAWSON. That is correct.

Senator GORE. Now, it seems to me that is significant because if there is a widespread campaign by the cable television industry to publicly denigrate the satellite dish industry, it serves as the clearest, most powerful evidence that the cable television industry does feel that satellite dishes are a potent source of potential competition. And therefore efforts by the cable television industry to require programmers in their negotiations with Mr. Phillips and others to raise the price at the wholesale level for satellite dish customers is motivated by the same thoughts. In other words, let's kill the competition so that we don't have constraints on the price gouging that we heard about yesterday.

Mr. DAWSON. That, sir, is the connection that we are here to try to make to the Senate today.

Later we went to court to find out why all these different cable operators all decided to run the same kind of hit ads against this emerging technology at the exact, same time. And in one case down in Arizona where they put the dealer out of business, of course, it was stated in a deposition that the advertisements, which have been discontinued since the court case, were based on cartoons supplied by Turner Broadcasting Company, and the scrambling schedules of possible signals in the future that I guess that they would control or whatever.

These ads are still going on. This happened just last year—excuse me—just this past year by ATC in New York. This is an ad to drive a satellite dealer out of business. It's facts you should know about satellite. And, of course, nobody knew that the cable company was the one who ran the ad. We had to find that out.

Well, one of the points that this ad drives home, which is true if ads like this prevail, is that many satellite dish companies go out of business within three years. I mean, what could be scarier? Well, they were right. They ran the guy out of business. So, I guess in that sense the ad was true.

But this is still happening and there is a direct correlation between an orchestrated program to attempt to suppress a viable, exciting technology that could be a competitive threat and an orchestrated program on another level to convince the citizenry that the signals are only available through the cable operator and that an orchestrated programming to adjust and distort the price to distributors so that becomes true. It is like the self-fulfilling ad of putting the satellite dish out of business. Well, when they put Mr. Phillips here out of business, then they will say, see, you can't do it. Only the cable can do it right.

Senator GORE. Well, we heard yesterday—and I am going to get to you in just a moment, Mr. Schmidt—about the dramatic rate increases by cable systems. And we heard the cable industry say or claim that competition was available. But here we have powerful evidence of an organized effort both through the control of programmers' prices at the wholesale rate, refusal to deal, an insistent refusal to deal, with distributors that are not controlled by the cable industry and through an organized public relations campaign to denigrate the competition, to really shut off competition.

Now, you have experienced some of the same problems, haven't you, Mr. Schmidt?

Mr. SCHMIDT. I just want to comment on some of the perception of this dialogue you have just been in the middle of.

The issue is not limited to a programming entity who is vertically integrated with the cable operator. I think it should be understood that the issue here is leverage. And ESPN, who should be distributing their product to everybody because they are selling an advertising supported service, you would think should sell without any encumbrance to any competitor, backyard dish, SMATV, wireless cable or direct broadcast satellite.

What has to be understood is that in order for ESPN to achieve its financial success when it acquires major league baseball rights and pays a substantial amount of money for the rights to Sunday Night NFL Football, integral to the success of that plan is an assessment program whereby the cable operator will then ante up an additional sum of money. In the case of NFL football, I think it was $3. And that is the leverage that the cable operator holds on ESPN.

I believe that ESPN really wants to sell to everybody. They have all the economic motives to do so. It is all there. Why don't they do it? It is clear because the leverage, the pressure of your customer, says if you do it, I might not pay you the $3.

So, ESPN, Disney, USA, anybody who is an independent source of programming is crying out for someone to do something. They want you to be a cop. They want you to step in and say the next time you do that, we are going to do something to you. We have to counter the leverage that is in this equation. It is a fundamental issue.

Now, I am not taking anything away from the basic premise of backyard dish or any other competitive technology. I want to compete. The bottom line is we are all would-be competitors in their eyes. We are trying to establish a beachhead to compete. And if you can keep people from getting on the beach, then you will never have competition.

The real threat in their mind is a twofold threat. It is direct broadcast satellite, and it is the telco. But neither of them will ever happen if cable—and you said it earlier in your own comments—controls the product.

So, I asked a cable operator last year sometime after Dr. Malone bought the Tempo service and acquired the rights to put in a KU satellite, I said, "did John Malone invite you into that deal yet?" He said, "no." I said, "well, maybe you won't be around." I said, "you better have a backup plan."

The bottom line is in the concentration process that is going on right now, the big are getting bigger, and the little are going away. So, therefore, competition is even an issue within the cable industry.

There is a fundamental point I want to make here though. The National Cable Television Association is an association representing primarily cable operators, but they represent programmers and hardware vendors within that group. I believe that all the leverage is still in the funnel, and if I control the distribution, then I don't care who you are. You have got to go by my toll booth. The next best thing for me to do, if Congress is going to shake that up and put other people in the position to have distribution, is to control the product. And that is where they are going.

Put the brakes on them. Make them divest if they won't cooperate with the marketplace. But the bottom line is the consumer needs an alternative choice, and they are crying out for it.

Senator GORE. We hear a lot about monopolies. We don't hear as much about monopsonies. The power of a single seller, the power of a monopoly, is pretty familiar to people. The power of a single buyer, a monopsony, is not as familiar outside the economics profession. The cable industry is both. And the power exerted by the cable industry over programmers comes not only by virtue of ownership and partial ownership, it also comes, particularly in the case of independent programmers like Disney and others—it can less so with Disney, but in the case of those who don't have the reputation and goodwill and product of Disney, it comes from the fact that the cable industry may provide 95 percent plus of all the revenue coming in to the programmer. And so, the leverage you spoke of exists.

Well, let me say that we are going to have to——

Mr. SCHMIDT. Could I ask one favor please, Mr. Chairman?

Senator GORE. Surely.

Mr. SCHMIDT. In an earlier statement made by Chairman Sikes, there was a reference to the study that the FCC is doing on the economic impact of the backyard dish marketplace.

Senator GORE. Right.

Mr. SCHMIDT. I don't know whether this is feasible, but we would be more than happy to cooperate in that same kind of economic impact study on the wireless cable industry. So, if that is feasible, we welcome that opportunity.

Senator GORE. All right, very good.

Mr. DAWSON. Mr. Chairman, I am sorry for the interruption. Can I note that this tape will be made available as part of the record? And there is a transcript with my testimony.

Senator GORE. We will receive it and consider it for that purpose. I am personally interested in hearing it. This is the Pat Robertson tape.

I am familiar with the letter that you referred to earlier, and I have always found it to be curious because Pat Robertson at that time had several motives for wanting as many viewers as he could get.

He was preaching the gospel and understandably wanted as many ears to hear that message as possible. He was selling advertising, the rates for which depend upon the number of viewers of that advertising. He was running for President and though not officially running at that time, wanted as many people to see him as possible. And he was raising money through heartfelt pleas to the listeners of his signal.

The 2 million plus satellite dish owners, mostly in rural America, are I think it is safe to say generally more likely to be responsive to Pat Robertson's message than city dwellers. Maybe I am wrong about that, but I think that on a percentage basis, he probably strikes a more responsive chord in rural areas than in big city areas.

So, why would he unilaterally deprive 2 million rural viewers of his signal, of the opportunity to see and hear his message? Curious, curious.

One possible explanation is the one which he himself offered, namely, that he was intimidated, frightened into scrambling his signal and taking it away from the rural viewers on satellite dishes by the threat of being removed from cable systems where most of his viewers gained access to the signal. If what he said initially is true, that would be evidence of the rawest form of economic power used to hurt a competitor, the competitor being the satellite dish industry.

Now, that is my understanding of what happened there, and I think that is your understanding of what happened there. Is that right?

Mr. DAWSON. I got that right from his voice and it is on this tape. That is what he says happens there.

Senator GORE. You didn't bring a tape recorder with you? You didn't bring a player with you?

Mr. DAWSON. No. I thought that the Senate——

Senator GORE. All right, fine. I'll listen to that with great interest.

I would note one other thing, Mr. Dawson. In my questioning of Mr. Malone yesterday, I said, "Do you think that the satellite dish owners are getting a raw deal where the decoders are concerned?"

Mr. Malone said, "Unfortunately, I think so, yes."

I said, "How should we help them get some justice where the decoders are concerned?"

Mr. Malone said, "I really don't have an answer. I've asked my people to think about what could be done. I hope that some solution will come there."

But if the decoder industry remains in turmoil and if decoders are hard to get, then this furthers the desire of the cable television industry to frustrate the development of the satellite dish industry. So, I am not going to hold my breath waiting for TCI to solve this problem, although they might surprise me and come up with a suggested solution. I will look forward to that.

We thank you for appearing here today. Thank you very much.

Our last panel is made up of Mr. Kent Foster, President of GTE Telephone Operations, and Mr. Dean Swanson, Chair of the United States Telephone Association. I wish to express my thanks to these two witnesses for their patience in coming at the end of a long hearing. But we await your testimony with undiminished interest.

Let me ask our guests to move from the room quietly, and the others who are arriving to do the same.

Without objection, as with the other witnesses, your statements will be included in the record in full. Thank you sincerely for your patience in sitting through the long proceeding today. We are very interested in what you have to say. We look forward to it, and if you could summarize your statements prior to the questions, that would be helpful.

We will begin with you, Mr. Foster, President of GTE Telephone Operations based in Irving, Texas. So, please proceed.

STATEMENT OF KENT B. FOSTER, PRESIDENT, GTE TELEPHONE OPERATIONS, IRVING, TX

Mr. FOSTER. Thank you, Mr. Chairman.

We are here today because the competition envisioned in the Cable Act of 1984 has not materialized and also because one of the key players in the delivery of telecommunications, the Nation's telephone companies, have been kept out of the video programming business.

We believe that the telephone companies' entry will provide the competition and technology necessary to bring new and innovative video services to America's homes and businesses.

And, I believe this point is particularly critical. It will also allow for the continued evolution of the Nation's public switched network, a network which is vital to the growth of our Nation's economy.

We have the opportunity to develop this network based on emerging technology which will provide many new capabilities. Many people have talked about this already. It will change the way in which we work, where we work, the way in which we provide education, health care. It will also change the way we market and purchase goods and services.

These innovations will become available to the American public through competition, not through reregulation of the CATV industry.

Our telephone network today is still the best in the world, but we are approaching a crossroads. A new generation of technology based on fiber optics and broadband switching can revolutionize the services that are available to customers.

However, the regulatory and legal barriers, some of them created to foster the development of the CATV industry, now stand in the way of the deployment of a nationwide broadband network. Certainly today's concentrated, large CATV companies don't need the legislative protection they currently receive. The distinction between cable television and telephone service embodied in the Cable Act of 1984 is quite frankly rooted in old technology with distinct services being provided over separate networks. Today's digital technology is moving us toward common delivery of all services over integrated networks. Outmoded, artificial barriers cannot and should not constrain the evolution of technology in the local network.

Now, even though the Cable Act of 1984 did not explicitly state a broad telecommunications policy, it implicitly favored fragmented special purpose networks. One of these networks is almost exclusively devoted to home entertainment. Investment decisions will continue to be made by communication service providers, including telephone and CATV companies. But the Cable Act certainly artificially skews investment decisions away from the integrated public switched network that is available to all and has a requirement to carry everyone's message, to fragmented special networks under control of a few.

Mr. Chairman, I respectfully submit that our Nation would be better served by a policy encouraging the development of an integrated switched broadband network available to all with a requirement to carry all messages and provide advanced services to everyone throughout this country.

GTE is working hard to bring that future closer to reality by constructing and operating a fiber optic network in Cerritos, California. We are also testing interactive video services and information services as a result of our efforts, which have only been underway for a few months, as we had to seek FCC approval. The equipment sizes have been reduced and other significant technological developments have occurred.

One has been developed by our own technical laboratories, and it is a broadband digital switch. This computer chip—and I think Chairman Sikes this morning referred to our demonstration in Boston of switching video channels—can switch a large number of video channels and be connected to an equally large number of customers. And you can stack these chips, any number, in a cabinet, and serve video requirements just like today's voice network serves voice requirements. This is standard CMOS technology, $200 a chip. (CMOS technology actually breaks out at approximately $10.00/chip.) It is not a pie in the sky or a unique laboratory development that will not be available to the American public for a decade or two decades as many people have alleged. It is ready now, and we are going to be putting this in service in Cerritos, California in the first quarter of next year.

We have the necessary technology today, but it won't be quickly and widely available unless the telephone companies are allowed to provide video programming. Our network will be available to all under the same terms, prices and conditions, but we need to assure that if we build these networks, it is going to be used. Telephone companies are not permitted to do that, as you well know, under the Cable Act today.

So, what needs to be done? The current restrictions against video programming or affiliation with programmers by telephone companies in their franchised area, often referred to as a cross-ownership band, must be lifted. And that is why we support your Bill S. 1068 which would lift the ban subject to safeguards.

Another legislative change we are recommending is that the franchise requirement for a video programmer be revised. We believe that requirement historically has applied to facilities and not to content and should be revised accordingly.

Lifting both these artificial barriers will greatly accelerate the deployment of a standard switch broadband network which will increase consumer choice. And success will then be determined by the market, not by arbitrary rules or restrictions.

We appreciate your giving us the time this morning to make this brief statement and we will certainly be happy to answer any questions at the appropriate time.

[The statement follows:]

Testimony of Kent B. Foster

PRESIDENT, GTE TELEPHONE OPERATIONS

I. INTRODUCTION AND SUMMARY

On behalf of the company I appreciate the Subcommittee's kind invitation to share our knowledge and experience with you as you approach the important issue of the role telephone companies can play in providing video services to the American public.

We have the opportunity to develop a communications network in this country, based on new technology, which will provide homes and businesses a wide array of new capabilities. Some of these capabilities, such as video on demand and high definition television (HDTV), will revolutionize the market for the delivery of video entertainment to the home. But that is only part of the story: other features of this intelligent network will change the way we work, and give us more freedom to choose where we work, will open new opportunities for education, and will allow us to receive better health care at lower cost. It will open new markets for goods and services, to be purchased at the touch of a button in our own homes. The intelligent network will fuel the engine of computer technology which has been the main driver of American competitiveness in the world economy.

GTE and other local telephone companies stand ready to make this intelligent, nationwide network a reality. Indeed, the process of development already underway in our existing network is laying the foundation for the network of the future. Mr. Chairman, I am not here to ask for a government subsidy to help create this new infrastructure. I ask only that we be allowed the freedom to develop our business along the path that technology and market forces are setting out for us. The United States has maintained its high standard of living, and its position in world markets, through the efficiency of our market system to create new technology. In years past, these strengths have helped us to build an infrastructure that includes the finest telephone system in the world. This infrastructure, in turn, has multiplied our strengths in all of the many industries which depend upon it. The ability to exchange information has improved the efficiency of our markets. Telecommunications and computer technology have combined to give birth to new industries, and to improve the efficiency of existing ones.

Our telephone network is still the best in the world today. To keep it that way, our industry can never afford to stand still. The equipment in the network is constantly being upgraded and, if necessary, replaced as new technology becomes available. As the capabilities of the network have increased, and as computer and telecommunications technologies have converged, it has become necessary to reassess existing regulatory boundaries, as the FCC has attempted to do in its Computer Inquiries.

Today the United States is approaching a crossroads. A new generation of technology, based on fiber optic transmission facilities, broadband switching, and software control, promises to revolutionize both the services available to consumers and the productivity of our industry. But, for the first time, our ability to maintain our leadership position in telecommunications is in question. Regulatory and legal barriers, some of them created to foster the development of segments of the communications industry, now stand in the way of the deployment of an intelligent, nationwide broadband network.

In particular, the distinction between "cable television" and telephone service, embodied in the Cable Act of 1984 and in the FCC's rules, has its roots in old technology, in which distinct, and somewhat limited, services were provided over separate facilities. The essence of the new technology is integration: the ability of a broadband network to provide different services, including voice, data, and video simultaneously, and the ability of the customer to control the network, using the same bandwidth for different functions at different times. If the United States wants a future telecommunications network that is pre-eminent in the world, it cannot remain simply a "plain old telephone" network.

Other nations are not shrinking from the challenge of new technology. A few years ago, the government-owned telephone authorities of Europe and Japan viewed with concern the U.S. movement toward a pro-competitive telecommunications policy. They worried that our dynamic market would leave them behind. Today, foreign telephone authorities are making bold investments in broadband technology and it is we who are being left behind. Today we find that portions of our national infrastructure, such as our roads and bridges, have deteriorated to the point where urgent efforts are required to bring them back to minimum standards. Tomorrow, if we allow ourselves to stand still, we may also find that our telecommunications infrastructure has fallen below the standards of those in other nations with whom we compete in world markets.[1]

The same legal barriers which stand in the way of new technology in the telephone network here in the United states have also inhibited effective competition in the markets they protected. We are all here today because this is precisely what has happened in the cable television industry. Sheltered from competition by the telco/cable cross-ownership ban, cable companies have expanded to serve more customers, as was intended. However, in terms of the quality, variety, and price of cable service, the hoped-for results of the current policy have not materialized. Perhaps most importantly, the cable industry has failed to create the open market for the exchange of video programming that the Cable Act envisioned. Instead, the cable market has been characterized by interlocking cross-ownership arrangements and self-dealing. The result has been to deny consumers the diversity of choice that a vigorous, open market would bring.

Mr. Chairman, GTE does not ask that federal policy be turned away from the pro-competitive philosophy which has guided it in recent years. On the contrary, we seek the removal of obstacles to competition. Specifically, I am recommending that Congress should:

1) Eliminate the ban on telephone/cable cross-ownership, both in the Cable Act and in the FCC's Rules.

2) Modify the current guidelines on local franchising to explicitly separate video transport from programming. Video transport providers would be franchised by the same local authorities who franchise cable operators today. Programmers would then be free to use these transport services. Programmers, or packagers of programs, would not be required to seek a franchise.

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[1] A policy statement of last August from the National Governor's Association noted the importance of the telecommunications infrastructure: "...The ability to transmit and process information is essential to improving economic productivity and growth and is playing an increasing role in the delivery of education, health care, and other essential social services.. This ability, in turn, depends on the capabilities, quality, and cost of our national telecommunications infrastructure...Indeed, our future social and economic health will depend substantially upon our nation's success in building a telecommunications system the equal of any in the world."

I do not make these recommendations for the purpose of allowing GTE to enter the cable television business as it exists today. Today, cable operators control a limited number of delivery channels, and determine what programming those channels will carry. Often, the cable operator also has an ownership interest in the programming. The intelligent network we foresee will have a virtually unlimited capacity to provide access to different program sources. This will allow us to offer transport services as a common carrier, at tariffed rates, to any program provider. Where we are able to add to the diversity of programming available on our network we will do so, most likely through joint ventures with existing firms with programming expertise. Any programs in which we have an interest will pay the same tariffed rates to use our network that other programs do.

Rather than replicate today's cable business, we simply want to pursue our own business, which is telecommunications, as far as the new technology will allow, to meet the demands of the marketplace. We are excited about the prospects the technology holds for our business, for consumers, and for the growth of our economy. We are also concerned that if we do not build the best communications network that technology makes possible we will lose, over time, our ability to compete effectively in the dynamic voice and data markets of the future. The telephone industry cannot afford to stand still. Yet current policy impedes us from moving forward. We must pursue the best available new technology to remain the best in the world in voice and data services. Yet, that same technology, the integrated broadband network, is also the most effective means of providing a full range of video services. To be economic, this integrated network must be allowed to provide all the services of which it is capable.

Unfortunately, if we built such a network today, present law would effectively prevent it from providing this full range of services. I am convinced that the achievement of the stated policy goals of the

Cable Act depends critically on the elimination of the cross-ownership restriction. The switching and transmission of information, rather than programming, is likely to remain our core business if we construct the intelligent network I envision. But, given the current restrictive nature of the cable industry, I do not believe that we can reasonably invest in that network, and provide effective competition in video transport, unless we also have the option of providing or arranging for programming on that network. It simply is not rational for us to walk into the world of cable television, as it is structured today, and expect the participants to use our network. We must have some effective means of sustaining our entry through a reasonable expectation that our network will be used.

I believe that the policy changes I have outlined will make possible a new and much more advanced telecommunications infrastructure in this country. This infrastructure will make our economy more productive and better able to compete in world markets. It will bring to consumers a wide range of services, of which video services will be an important part. Provision of video services by telephone companies will dramatically open the video market, permitting, for the first time, the free exchange of video information. We will do this, not simply by providing a competing, alternative wire to the home, but by providing a more capable network which will fundamentally change the restrictive conditions that characterize the video market today. We will, of course, face strong competition from cable operators who are already entrenched in their markets. This competition is the most effective way to remedy the problems in the cable market which have given rise to this hearing.

II. GTE AND TECHNOLOGICAL DEVELOPMENT

A. GTE'S VIDEO EXPERIENCE

GTE's abilities and experience in providing first rate telecommunications services are well known. GTE's corporate history includes the operation of cable television systems. In the 1960's a GTE subsidiary, GTE Communications, Inc. ("GTEC"), operated more than 50 cable television systems in 10 states, both within and outside of GTE's telephone operation territories.[2] Another GTE business unit (GTE Lenkurt) manufactured set-top converters and other equipment for the cable TV industry. As late as 1981, a GTE telephone company provided channel service facilities to a cable operator. However, channel service offered by telcos to cable companies is rare. In the last 15 years most cable operators have chosen to enter into contracts for the use of telephone company or power company poles and to serve their customers via their own distribution plant (coaxial cable.)[3]

Today, in a rapidly developing technological environment, GTE maintains a presence in the video world. GTE Spacenet, for example, provides broadband transport for some video programmers and some interactive services, such as video conferencing. GTE has also provided video services to broadcasters televising such events as the 1984 Olympic Games in Los Angeles, the Super Bowl and the national political conventions. Finally, GTE Laboratories has long been active in researching video transport systems, transmission-reception technology and channel capacity for the development of advanced broadband networks. Our most visible video-broadband project has been our coaxial/fiber/copper test bed in Cerritos, CA.

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[2] California, Florida, Georgia, Illinois, Indiana, Michigan, Pennsylvania, Texas, Washington, and Wisconsin. GTE left the cable business between 1970 and 1974 as a result of the FCC Rulemaking establishing the cross-ownership rules.

B. TECHNOLOGY ADVANCES AND THE TELEPHONE INDUSTRY

GTE's involvement in the development of broadband technology is the natural extension of a tradition of technical innovation.

The telephone industry has provided the leadership and expertise that permitted the telecommunications sector of the economy to make rapid and profound advances in productivity. The evolution in telephone switching technology from manual to Strowger to step-by-step to crossbar to electronic to digital is not only a recitation of improved telecommunications capabilities, but it is also a statement of our industry's commitment to better service and productivity.

The same technical change that has brought new services and improved productivity has also generated market pressure for changes in both industry structure and public policy. The development of microwave and satellite transmission and the resulting changes in national telecommunications policy permitted an increasing number of long-distance providers to compete. Although the transition to this competitive environment has not always been smooth, it is clear that having additional suppliers in the interexchange marketplace has meant more choice for consumers and increased pressure on suppliers to provide the widest array of products at the most attractive prices possible.

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[3] Present fiber experiments may make channel service a more common option for CATV firms. In addition to GTE's Cerritos experiment, see also, Southern Bell's Heathrow (W-P-C-5931, W-P-C-6166) and Hunter's Creed (W-P-C-5803), Bell of Pennsylvania's Perryopolis (W-P-C-6246), Southwestern Bell's Mira Vista (W-P-C-6417) and Cincinnati Bell's (W-P-C-6475) project with Warner Cable in downtown Cincinnati. These fiber trials may offer exciting new transport possibilities for cable operators.

C. IMPORTANCE OF NEW TECHNOLOGY TO U.S. ECONOMIC INFRASTRUCTURE

The new generation of technology, including fiber optics, holds the promise of similar benefits in the market for local distribution of voice, data and video. It offers increased capacity, new services, and higher productivity. Further, just as microwave and satellite transmission made it possible to have more than one supplier of long distance service, fiber is making it possible to have more than one supplier of local distribution for all services.

The development of new technologies is important to the U.S. economy and consumers. New and more efficient services provided by the telecommunications sector of the economy provide benefits throughout our economy. A vibrant, healthy telecommunications infrastructure that fully satisfies the needs of a modern information society cannot help but assist and enhance the competitive position of the U.S. vis-a-vis our foreign technological competitors.

Mr. Chairman, your Subcommittee and this Congress can create an environment through legislation which will encourage the development of new technology and ensure the greatest possible benefit for the American consumer from this new technology. That is why I am here asking you and your Subcommittee to make possible a marketplace which encourages the development of technology, and that brings to American consumers the broadest variety of services in the world.

There are certain conditions necessary for making the investment in new broadband facilities (fiber optics) to the home. Simply, it is vital for information and video entertainment to use such a network. In order to take the risks inherent in constructing such a network, telcos will need some assurance that users will be there. We cannot simply build this network as a passive common carrier and hope users will find ingenious means of using it. This is likely to be a vain hope, given the current nature of the cable programming market, which is characterized by close ties between program providers and cable operators. We need a market structure which allows telcos to demonstrate the new network's potential being permitted to sell some of the services we know have great market appeal.

D. THE NEED FOR LEGISLATION

There are numerous pieces of legislation pending before your Subcommittee that attempt to deal with perceived competitive problems in the cable television marketplace. The most comprehensive of these regarding telco participation in cable television is S. 1068, introduced by Senators Gore (D-Tennessee), Gorton (R-Washington), and Ford (D-Kentucky). GTE believes that such legislation is congruent with technological and market realities. I would like to explore in depth with you how technology in telephone networks, specifically fiber optics, can help resolve current cable market imperfections and lead to vigorous development of information services. Although the relatively narrow world of video entertainment and telephone company entry into cable is the subject of these hearings, GTE maintains, Mr. Chairman, that the Gore/Gorton legislation moves in a direction that will have important ramifications for all telecommunications sectors.

III. NEW TECHNOLOGIES FOR LOCAL DISTRIBUTION

GTE has developed a long term vision of the telecommunications environment of the 1990s and beyond, and the type of network that will be required to succeed in that environment. The future network will be based on developments in optical fiber, microelectronics and software, with a gradual integration of telephone network architectures and computer architectures. The software "control" to manage the network will be separated from basic switching and transmission functions. This software control will allow our customers to configure the network capabilities they purchase from GTE to suit their needs.

These advances in technology are redefining the nature of GTE's network. Yesterday, we provided plain old telephone service ("POTS"). Today, we offer a wide array of voice and data services. Tomorrow the same network that carries voice and data more efficiently will also make information and video services possible.

Rather than discuss all aspects of the new technology in detail, I would like to focus today on one development in particular - fiber optics - which will play a crucial role in the intelligent network of the future.

A. ADVANTAGES OF FIBER TECHNOLOGY

Fiber optic cable has become the medium of choice for transmission of voice, data, and video signals, because in most applications, it is more cost effective and provides higher quality service than the older copper technolgy.[4]

Fiber is cost effective today wherever information must be transmitted at high speed or in large volumes. The bandwidth available on a fiber system is limited mainly by the opto-electronic equipment on each end. The capacity of a fiber transmission system can therefore be expanded by upgrading this equipment. These upgrades are usually much less costly than adding new copper-based transmission facilities of equivalent capacity. Over time, new generations of opto-electronic equipment will continue to be developed, each providing greater capacity over the same fiber cable.

Fiber transport also provides a high quality digital signal that is virtually impervious to electromagnetic interference. This quality advantage over copper transmission systems has become more important as our network is used increasingly to transmit data which is sensitive to such interference.

B. FIBER AND THE EVOLUTION OF NETWORK ARCHITECTURE

In a traditional telephone network, every subscriber is connected to a central office by a pair of copper wires. The intelligence in the network is provided by the central office switch, which directs calls according to the digits dialed by the subscriber.

Today our network is evolving toward a distributed architecture where the copper wire service each subscriber terminates, not at the central office, but at a remote device positioned as close to the subscriber as possible, usually no more than 12,000 feet away.[5] The traffic generated by all the subscribers in each neighborhood is concentrated at this device so that it can be transported to the central office on a shared, high capacity facility.

The intelligence in our network is also becoming more widely distributed. Some of the switching in the network is performed in the remote devices I have described, acting under the control of a central office host. The central office switch, in turn, will be increasingly controlled by software and data bases which will be located wherever it is most efficient to place them.

Today we are already using fiber optic facilities to connect central offices with one another, and to link each central office with the remote devices I have described.

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[4] When these remote devices perform switching functions under the control of the host central office, they are called remote switching units ("RSUs"). When these devices perform no switching, but simply concentrate traffic, they are known as remote line units ("RLUs").

[5] GTE does not simply assume that any one technology is always best. This is why, in our Cerritos experiment, coaxial cable and twisted pair technology is being explored along with fiber.

We have also placed fiber directly to the premises of customers whose needs include high capacity data applications. At the end of 1988, GTE had a total of 185,000 fiber miles installed in its network.[6] By 1994 we plan to have over 500,000 fiber miles installed.

C. EXTENSION OF FIBER CLOSER TO THE CUSTOMER

This distributed architecture, with signals carried close to the customer via fiber, is helping GTE to provide an expanding array of voice and data services at lower cost and with higher quality. Soon, for example, we will be using it to provide Integrated Services Digital Network ("ISDN") services to our customers.[7]

Beginning in 1992, the next stage in the evolution of our network will see fiber carried out to a second generation of remote devices which will be placed within 2,000 feet of the customer. We are working with manufacturers now to develop this device, which we call an Enhanced Remote Line Unit ("ERLU"). The ERLU will be connected to the central office via fiber using the standard industry protocol, Synchronous Optical Network ("SONET"). The ERLU will be an active electronic component providing enhanced operations, administration, maintenance and service provisioning by remote control from a central location.

All of this equipment is being designed so that it can gracefully evolve to accommodate broadband video transport. This will involve placement of fiber in the last 2,000 feet of loop facility that connects the subscriber to the ERLU. Completion of an all-fiber network will further improve signal quality by removing the last

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[6] Fiber miles are calculated as the number of fibers times the distance, so that we would have the equivalent of 185,000 miles of cable if each cable had only one fiber.

[7] GTE has several narrowband ISDN tests operating in North Carolina, Florida, and Texas.

analog segment from the transmission path. It will permit a wider range of data and information services, as well as video services, to be made available. It is the last step in the evolution of the integrated broadband network of the future that will depend most critically on the policy decisions made by this Congress.

D. CATV FIBER V. TELCO FIBER

While the fiber-optic facilities being installed by LECs and CATV operators are similar, the network architectures are not. Each network has been optimized for a different range of uses.

The typical CATV network is an arrangement where each house is connected via a coaxial bus that is common to all drops and is connected to the cable system head end by a coaxial or cable trunk. This bus cable carries all TV channels to all houses via frequency division analog transmission signals. This is the optimum arrangement for sending a few broadband signals to many users simultaneously. This network becomes strained when the demand for more channels exceeds its capacity.

In its simplest form, the typical LEC network consists of an individual dedicated circuit for each house tied to a central office matrix-type switch that can interconnect any two circuits, including trunks connected to other central offices. This more flexible arrangement is optimum for sending discrete signals to individual users.

The network evolution described in this section is driven by the increased cost of copper wire as well as the increased demand for bandwidth for high speed data and other applications. Both networks are installing fiber-optic cables to gain cost effective bandwidth to meet increased demand.

We believe that there is a demand for real time switched broadband services that are not compatible with the 'bus' architecture used by CATV systems. Whether provisioned via coaxial cable or fiber, the CATV system will always be constrained by a limited number of channels. By breaking this limitation, the switched architecture of the broadband telephone network offers an opportunity for a truly open market in which each subscriber has a vastly expanded range of choice, and anyone who creates a program can sell it to any subscriber.

E. VIDEO SERVICE CAPABILITY IS NATURAL OUTCOME OF TELEPHONE NETWORK EVOLUTION

I have reviewed our network development plans with you in some detail in order to emphasize that the provision of video service over fiber facilities is a natural outcome of the technological evolution of the telephone network. Much of the discussion of the telco-cable cross-ownership issue has focused on a "second wire" to the home as if the telephone network did not already exist. Some have suggested that the telephone industry wants to build a new broadband network, at great cost, specifically for the purpose of duplicating cable systems.

In fact, the existing telephone network is already rapidly developing to provide the basis for a broadband, fiber network. Given an appropriate public policy, this evolution will naturally -- and efficiently -- include video capability. The broadband network of tomorrow will not involve the construction of a new network. It will be built on the solid base of today's network as part of the ongoing development of that network.

The difficulty we face is that the appropriate public policy to permit this network is not in place today; yet we must press forward with our network planning. Each year we make substantial investments to improve our network. As I have described, we try to plan our network improvements today so that they will support the broadband network of tomorrow. At some point, however, choices must be made.

We believe that significant economies will be made possible by the integration of voice, data, and video on a single network. To realize these economies, however, we must make substantial investments over the next few years. We believe that these will prove to be sound business investments for the company, and wise investments in national infrastructure from a public policy standpoint -- if the integrated network is allowed to provide all the services which it is capable of providing.

However, the imperfections in today's cable market make it likely that the video capabilities of our integrated network would not be fully used. This creates an unacceptable risk for us that, having invested in a wide range of network capabilities, we would effectively be limited to a subset of those capabilities. The option of arranging programming for our own network would allow us to reduce that risk, but we are prevented from doing so by the cross-ownership ban. Further, current franchising arrangements would prevent us from providing video transport to programmers other than the incumbent cable firm.

Mr. Chairman, GTE is prepared to accept the normal business risk inherent in any investment made in a competitive market. But the risk we face in the video market is vastly increased by the non-competitive nature of that market today, and by public policy which serves to keep it that way. If these policy changes are not implemented, it will be very difficult to justify the investment needed to make the integrated network of the future a reality. Since the same new technology addresses future needs in voice, data, and video, failure to move ahead in video technology may lead the United States to fall behind in voice and data services as well.

IV. THE INTELLIGENT BROADBAND NETWORK WILL OPEN THE WAY FOR A VIRTUALLY UNLIMITED VARIETY OF SERVICES

A. THE CERRITOS TEST BED

GTE bases its network implementation plans on a realistic assessment of both technical and market realities. Important questions facing us are: what is technically feasible, and what does the telecommunications user of the late 20th century desire? GTE is currently seeking the answer to these questions and several others in an exciting project in Cerritos, California.

In February of 1987 GTE California submitted a Section 214 application to the Federal Communications Commission to construct, operate, and maintain a coaxial cable system for its customers, Apollo Cablevision and GTE Service Corporation. After securing approval of this application, GTE California then applied to the FCC for permission to construct a fiber optic network in a portion (approximately 1/3) of the territory served by the coaxial network. The FCC granted both the coax and fiber applications at its April 1989 Open Meeting.[8] GTE intends to conduct experiments relating to technical design alternatives for voice, data, and video on these separate networks. GTE will compare the technological and operational features of fiber, coax, and twisted pair copper service delivery systems. The Cerritos test bed will be a living laboratory where these technologies and services can be tested in a real world environment.

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[8] Memorandum, Opinion, Order and Authorization, File Nos. W-P-C-5927 and W-P-C-6250, FCC 89-127, adopted April 26, 1989, released July 17, 1989.

The Cerritos Test Bed consists of four phases:

PHASE I: Fiber and Coax Broadband facilities will be used to test voice, data and video transmission services.

PHASE II: Interactive Video Services such as home shopping and banking, educational services, and other information services will permit end users to access numerous services from the convenience of their own homes. Also, an enhanced pay-per-view service that allows customers to select from 28 channels of information, including various special events and entertainment, will be tested. Initially, Phase II services will be provided on the coaxial network and tested later on the fiber network.

PHASE III: Video On Demand will permit a customer to select any program from a large inventory and view that program at home at any time the customer chooses. This capability will open up a new world of choice for the customer, and a new world of opportunity for program suppliers, since neither will be limited to a few prepackaged channels.

PHASE IV: Point-to-Point Switched Broadband will test the capabilities of the fiber network to switch video from one residence to another. The same capability would permit video to be switched from any program supplier to any customer.

GTE believes that the Cerritos test bed will become a microcosm of a new information age in which the most sensitive and discriminating measurement tool -- the customer -- will help determine new technologies and services. For example, the city of Cerritos is planning to develop services that will let people use the system to register to use its tennis courts, sign up for recreation programs and get dog licenses or temporary parking permits.

B. IMPROVED INFRASTRUCTURE AND A MORE OPEN MARKET WILL STIMULATE NEW SERVICE DEVELOPMENT

While GTE expects to play a major role in the development of new services, it is important to recognize that the full benefits of the new information technology will not be realized solely through the efforts of a single firm. Rather, the creation of a competitive market, based on an efficient infrastructure, which permits the free exchange of information and services, will allow many different market participants to create products and services which will maximize the value of the new technology for the consumer.

The vast potential of the personal computer was realized, not only through the efforts of manufacturers like IBM and Apple, but also by users and third-party vendors who created countless programs, applications and hardware devices for these machines, many of them unanticipated by the manufacturers themselves. Had these manufacturers retained exclusive control of the programming to be used in their PCs or installed hardware enhancements, their products would have been much less successful.

GTE believes that an open market for data, information and video services will benefit customers by giving them a wider range of choices. As the builder of the network, GTE has no intention of controlling content, but rather seeks to encourage the use of the network. That is why I believe that promoting the development of a switched broadband infrastructure would be a primary goal of federal telecommunications policy.

As the Members of the Subcommittee are aware, our Cerritos proposal has generated much controversy and opposition from our friends in the cable television industry. GTE submits that these apprehensions are misguided at best and both anti-consumer and anti-technology at worst. GTE's objective in Cerritos is to find the most innovative and cost-effective ways of building and operating a broadband network and assessing customer reaction to some of the uses to which such a network can be put.

V. POLICY/LEGAL BARRIERS TO THE NEW INFORMATION AGE

Historically, (at least since 1970 and the imposition of the cable/telco cross-ownership rules) our traditional narrowband services have been separated from the provision of wideband video service. GTE believes that fiber technology promotes the convergence of these services and technologies. The Members of this Subcommittee have the opportunity to chart a new policy course that will enable telephone companies to make full use of the technology that the industry has developed to benefit the public.

A. THE CABLE INDUSTRY'S REMARKABLE SUCCESS

The original rationale for keeping telcos out of the cable business in 1970, i.e., to encourage a fledgling cable industry to develop, has succeeded admirably. Today, the cable industry is no longer a fledgling in need of protection; it has become a vigorous and prosperous player in the telecommunications field.[9] Cable television firms, with their entrenched positions and strong marketing skills, are well equipped to compete with any new entrants, including telephone companies.

It is curious that cable companies who have been the beneficiaries of one technological revolution now seek to inhibit the continued development of technology. In their earliest days cable companies provided mere retransmission of over-the-air broadcast signals, largely to rural areas outside of the normal broadcast signal contours. With the successful development of satellite-based programming in the mid-1970's, cable operators could hook up a satellite dish to their head-ends and receive a multitude of services (movies, over-the-air retransmissions, and other basic and pay cable services). The availability of programming encouraged operators to expand their channel capacity from 12 to 20 to 35 to 50 and now more. Furthermore, the cable industry and the investment community now had the incentive to wire the more densely populated areas of the country, the major cities. The cable industry set out to wire America and they have succeeded. Eighty-six per cent of all residential households in the United States are now passed by coaxial cable systems,[10] with more than half of the total U.S. households on the subscriber lists of cable operators.

As cable television has increased in popularity, firms with great financial strength have emerged as dominant players in the cable market. Group W., Cox, Continental Cablevision, TCI, and Time-Warner Communications all have contributed to the development of the cable business.

B. THE CABLE ACT OF 1984

The most significant policy milepost for the cable industry was the passage of the Cable Act of 1984 which created a new Title VI in the Communications Act. This legislation recognized the cable business as a major sector within the telecommunications industry, and sought to establish for the first time a national policy for cable communications. Two of the Cable Act's original purposes are

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[9] See, e.g., "With America Well Wired, Cable Industry is Changing," New York Times, July 9, 1989, p.A1.

[10] See "Prying Open the Cable-TV Monopolies, "Wall Street Journal, August 10, 1989, p. B1.

significant for our deliberations today. Section 601(4) asserted that the purpose of the law was to "assure that cable communications provide and are encouraged to provide the widest possible diversity of information sources and services to the public" and section 601(6) said the law was designed to "promote competition in cable communications and minimize unnecessary regulation that would impose an undue economic burden on cable systems."

C. IMPERFECTIONS IN THE CABLE TELEVISION MARKET

The cable industry grew rapidly and prospered in the protected environment that was formalized in the Cable Act. With the exception of sparsely populated rural areas, telephone companies were prohibited from operating or being affiliated with cable systems in their own franchised areas. The cable industry took advantage of satellite delivery and increased program sources in sports, news, and entertainment, to wire America. Further, the Cable Act has completely deregulated rates for basic cable service for virtually all cable companies.

Yet this success has brought with it unanticipated results which conflict with the stated goals of the 1984 Act. While the goal of encouraging the growth of cable has to some extent been achieved, the goals of promoting competition and encouraging the "widest possible diversity of information sources and services" have not been met. The untoward results of current policy include the following:

BASIC SERVICE RATES: In the absence of effective market or regulatory constraints, rates for cable service have rapidly escalated. The General Accounting Office reports that since most cable rates were deregulated in December 1986, basic rates increased on average by 29% per subscriber in little more than 21 months.[11]

CONCENTRATION: A series of mergers and acquisitions has greatly increased the concentration of ownership in the cable industry. The recently announced combination of Time and Warner creates a single company which will control access to 10% of cable subscribers nationwide.[12] The three largest cable operators today control the viewing choices of over one-third of the cable subscribers in the United States. The prices paid for cable properties in these and other transactions have skyrocketed. These increases in the value of cable systems set the stage for additional rate increases in the future as new owners seek to earn a return on their investments. Claims by cable operators that they lack market power are belied by the market evidence of the prices at which cable systems are traded. Recent transactions have seen prices in excess of $2,500 per subscriber. What asset does a cable system have for which a buyer would be willing to pay that much? Surely, not their networks, which could be reproduced for much less.[13] Clearly these prices represent the capitalized value of the market power cable firms possess.

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[11] See GAO Report, National Survey of Cable Television Rates and Services, August, 1989.

[12] Numerous newspaper accounts have pointed out that the Time-Warner merger created the single largest entertainment in the world. It is interesting to note that in terms of number of subscribers the Time-Warner cable company will be dwarfed by TCI which controls almost one-fourth of the nation's cable subscribers. This is roughly twice the market share of the largest local telephone company's.

SELF-DEALING: Cable operators and program providers have become entangled in a bewildering web of self-dealing and restrictive special arrangements. Cable companies own program providers, and vice versa. Struggles have developed between interest groups over such issues as whether New York, New Jersey and Connecticut cable subscribers will get to see New York Yankee baseball games, or whether NBC's financial news network will be widely distributed in competition with a similar channel from Turner. NBC's difficulty in obtaining distribution appears to be related to the fact that certain cable operators participate in the ownership of Turner. (NBC's venture is also partly owned by cable firms).

Viacom has recently filed an antitrust action against Time-Warner for allegedly favoring HBO over Viacom's Showtime channel. Time-Warner is the second largest cable firm, with about 5.6 million subscribers. It also owns HBO, the most successful premium channel, which has 22 million subscribers.

Viacom, with about 1 million cable subscribers, now plans to sell half of Showtime, the second most popular premium channel, to TeleCommunications, Inc., ("TCI"), the largest cable operator, which has about 12 million subscribers. Time-Warner has threatened an anti-trust suit of its own, naming Viacom and TCI, to block the sale. It also happens that Time-Warner and TCI together control about 40% of Turner Broadcasting Systems, Inc., whose financial news channel I referred to earlier. Small wonder that a TCI spokesman has characterized Time's threatened suit as "the pot calling the kettle black."[14]

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[13] While there are very few sales of LECs, and even fewer in which terms are made public, these appear to be selling in the range of $2,000 - $2,500 per line - also above reproduction cost of the network but not so far as cable companies. Besides market power another reason for this price gap is regulation - or lack thereof in cable.

LIMITED CUSTOMER CHOICE: Because of the restrictive contractual and partnership arrangements which characterize the cable industry, the choices that cable customers have among programs are sharply limited. The choice of what customers are able to see, and when, and how much they will pay, appears to be determined by the affiliations among the suppliers in the industry, rather than by customers voting with their dollars in a free market. The typical cable customer is usually faced with the limited options of either accepting far fewer over-the-air channels or none at all. Further, the channels available on a cable system are usually offered only in carefully contrived packages of basic and "premium" services. Because of this "bundling" a customer will frequently have to pay for several channels he does not want in order to obtain a particular channel.[15] Similarly, the difficulty of gaining nationwide cable distribution is a strong disincentive to program producers. If wide distribution were readily available to all program producers at reasonable rates, it is likely that a wider variety of programming would be supplied.

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[14] See Multichannel News, May 15, 1989, p. 1; Wall Street Journal, October 25, 1989, p. B7

[15] A recent article discussing the potential of purchasing specific individual cable programs was dismissed by NCTA's President ("I don't think it will work..."). See USA Today, "Cable a la carte offers a menu for the '90's", June 20, 1989, p. 3D.

LACK OF SERVICE QUALITY: Consumers have been disappointed with the quality and reliability of cable service. A recent USTA Survey indicates that 50% of a sample of cable subscribers reported out of service problems in the past year v. 19% for telcos. Service was restored promptly in 70% of the CATV sample v. 87% for telcos. Significantly, 68% of cable customers felt service would be better with a competitor. Finally, a strong majority (57%) believed that LEC's should be competitive providers.[16]

FAILURE TO DELIVER NEW SERVICES: Finally, cable companies have failed to expand the range of services they offer beyond video entertainment and news. The FCC's cross-ownership rules of 1970 originally were intended to protect the cable industry and to foster the development of many new broadband services. In this 1981 Report on Cable Ownership, the FCC Office of Plans and Policy ("OPP") qualified its support of the cross-ownership rules by concluding that "if cable remains almost wholly an entertainment medium, the ban will serve little useful purpose and should be eliminated."[17] In fact, cable has remained almost entirely an entertainment medium, and the other broadband services the policy aimed to promote have not materialized.

Broadly stated, although cable has created a broadband delivery system, consumers have been denied the full benefits that broadband technology could bring because of the market imperfections I have just described. To a great extent, these imperfections are rooted in a fundamental condition which has always characterized the delivery of video signals in this country: the control of program content through the control of a limited number of delivery channels. In cable, the effects of this market constraint have been exacerbated by the pattern of cross-ownership and self-dealing between cable systems and program suppliers. Federal policies which have served to protect the cable industry have only entrenched the cable companies in this monopoly position by preventing competitors from entering. A new policy is needed if this pattern is to be broken and an open market for broadband services established.

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[16] See USTA Survey; Also, Mr. John L. Hanks, Director of Franchising in New York City has described ATC's customer access to customer service as "notorious", See New York Times, June 16, 1989, p. B3.

[17] See FCC, Office of Plans and Policy, "FCC Policy on Cable Ownership," November, 1981, 177; Comments of the GTE Telephone Companies, Docket 87-266, November 2, 1987, at 7-9.

VI. THE PUBLIC INTEREST/MARKET SOLUTION

A. COMPETITIVE ENTRY BY TELCOS WILL REMEDY MARKET IMPERFECTIONS

GTE believes that the most effective remedy for the problem I have described is competitive entry by telephone companies into the market for video services. Entry by the telephone companies will open up a market which is now tightly restricted. Consumers will benefit from a wider choice of entertainment programs, as well as the development of additional broadband services. Program providers will gain open access to subscribers at reasonable and nondiscriminatory rates. Competitive pressure will spur the development of new capabilities and will provide incentives for both telephone and cable companies to maintain high levels of quality and reliability.

Effective market participation by telephone companies would directly address the market imperfections I have described. The linkage between control of content and control of a limited number of channels would be broken by a number of factors. First, telephone companies would provide a competing supply of local distribution that doesn't exist today. Second, telephone companies would introduce a switched video technology under which the number of programs available to the consumer would no longer be limited by the number of delivery channels. This will greatly reduce the importance of the limited number of channels as a market constraint. Third, transport service will be available on an unbundled basis at tariffed rates to all other program providers, so that telephone companies will not be able to use control over delivery to favor their own programming.

Telephone companies have much to contribute to the market for local broadband distribution. Most significantly, telephone companies have knowledge and experience gained over many years with our existing local distribution network. This network, which has always had a two-way, switched architecture, is already evolving rapidly into an intelligent, highly capable, fiber-based system. Video capability is a logical step in this network evolution.

Building on this solid base of experience, GTE is looking into the future with its experiment in Cerritos, California, as customers there help us to develop the menu of services that an integrated broadband network will offer. This menu will include an expanded range of choice among entertainment video programs, as well as a variety of non-entertainment services which have not been forthcoming from cable systems. GTE invites this Committee to join us in our vision of the information age and hopes that through your leadership the Congress can help make the information age a reality.

GTE and other telephone companies would bring to the cable market a strong tradition of service quality and reliability. Telcos would also bring a long-standing commitment to meeting local community needs and providing widely available service.

Further, the telcos are accustomed to providing service to all customers who wish it. This is contrary to the experience of today's cable operators who have no common carrier obligations. If GTE were permitted to offer video programming to its subscribers, we would stand ready to provide non-discriminatory transmission service to other video programmers at the same tariffed rates.

B. TELCO PROVISIONING OF PROGRAMMING IS VITALLY IMPORTANT TO INJECT REAL COMPETITION INTO THE MARKETPLACE

Mr. Chairman, I believe that the policy proposals I outlined for you at the beginning of my testimony are crucial in achieving the competitive market outcome I have just described. Our two key proposals are the elimination of the cross-ownership prohibition and a modification of the law's franchising guidelines. I will discuss the cross-ownership ban first and then will provide my views on the franchising issue.

GTE is aware that telephone companies are free to offer channel service today. Why then, it might be asked, must the telcos be permitted to offer programming as well?

The simple answer is that the imperfections in the cable market today prevent effective competitive entry on the basis of transport alone. Given current local franchising arrangements, and the law, the existing cable company is the only possible customer for transport service. This means that telco entry would provide only an alternative source of transport supply for the cable operator, rather than effective competition.

Even if my proposed changes to franchising arrangements were adopted, the existing relationships between cable systems and program sources would still preclude effective entry. The cable operator is the incumbent provider of transport, and, through the pattern of cross-ownership and exclusive agreements previously described, cable systems also exercise a high degree of control over programming sources. Cable operators have every incentive to use this control to keep programming on their own systems, and to prevent it from migrating to telephone company systems.

In fact, while telco transport service has been possible for some time, relatively few transport arrangements exist. It is unreasonable to expect that telephone companies will be able to effectively enter the video transport market, so long as the cable industry has the power to prevent our networks from being used for potentially revenue producing applications.

Mr. Chairman, GTE sees its network as the core of its business. That is true today, and it will remain true as we seek to develop the intelligent, broadband network of the future. We do not regard programming as a new business to be pursued solely for its own sake. We also do not see ourselves becoming the dominant programmer within or outside the areas we serve today. There are numerous entities who are capable of providing video programming, and, if given the opportunity, we believe they also could be successful. In GTE's vision success in video programming should not be limited to entrenched CATV systems. However, we do believe that video will be an essential part of the range of services, both entertainment and non-entertainment, to which the network of the future will provide access.

This is why we see the elimination of the cross-ownership ban as crucial to the success of the new network technology. If, as we expect, the current imperfections in the cable TV market, including cross-ownership of programming and self-dealing by cable companies, work to impede other programmers from using our network, we will have the option of arranging programming to make full use of our network's capabilities. This is the assurance we need to make the investment that will be required to build a nationwide broadband infrastructure. To use a homely metaphor, Mr. Chairman, we will be willing to build the pond if we know beforehand that we can stock it, should that be necessary.

Under the market structure I have described, with competition from the cable company and with our transport available to anyone at tariffed rates, we will not be in a position to favor our own programming over that of any other provider. I must emphasize, however, that telephone companies will be able to provide effective competition in the cable market.

C. GTE SUPPORTS A MODIFIED FORM OF LOCAL FRANCHISING

It is interesting to note that organizations such as the National League of Cities, which represents local governments who serve today as franchising authorities for cable systems, have endorsed efforts to bring greater competition to the market for video services. These city and county governments have seen firsthand the deficiencies in the market in which their constituents purchase video services today.

GTE supports the concept of local franchising of telecommunications systems that deliver video systems to the home. We expect that, when we begin to provide transport for such services, we will seek franchises from the appropriate local authorities. However, some modifications to the franchising arrangements presently codified in Section 214 of the Communications Act will be needed if the competitive outcome supported by the cities is to be achieved.

Today, the cable operator is franchised both as a provider of transport and as a programmer. Although federal law does not require these franchises to be exclusive, many of them are. In return for franchise rights, cable firms pay franchise fees and provide certain amenities, such as public access channels and production facilities.

I believe that this basic structure can serve the public well if it is amended as follows:

Any entity that provides video transport should be required to obtain a local franchise. No franchise should be required for video programming. This separation is essential if the link between control of transport and control of programming is to be broken. The cable company, the telephone company, and any other firm that chooses to enter the transport market, would be franchised as video transport carriers. Each of these transport providers would also be able to provide programming, but firms providing only programming would not need a franchise.

This modification would allow competing firms to enter as transport providers, as video providers or both. It would ensure that the incumbent cable firm would not be the only entity that could supply programming to a competing telephone company transport system. And it would allow any program provider to use the transport service made available by the telephone company. I expect that, in addition to basic transport functions, GTE would also make available a menu of related services, such as billing and program listings, which would make it easy for any provider to package its product so that subscribers on our system would find it convenient to use.

Within this modified framework, I believe that the public interest obligations of the current franchise arrangements can be retained. For example, the franchised transport carrier could continue to provide amenities such as public access channels. The transport carrier could also either pay a franchise fee, which it would recover through its basic service rates to subscribers, or collect fees as part of the rates it would charge program providers for the use of its facilities.

Of course, GTE would also expect to comply with all applicable state and federal regulations. This would include state oversight of intrastate voice and data services provided on the same system. It would also include FCC regulation of video transport rates, over which it has already established jurisdiction. Another area which presently does not impose legal obligations relates to carriage of local broadcast signals. GTE would comply with any applicable "must carry" rule. The importance of local broadcast television in communities throughout America and good business sense dictate that GTE would provide free local carriage of traditional broadcast stations just as cable operators do today.

D. SOLUTION IS COMPETITION, NOT RE-REGULATION

GTE is convinced that only a public policy based on market competition will resolve current problems in the CATV market and will provide the incentives to build the broadband infrastructure that the U.S. economy needs.

What other policy would serve the public as well? Rate re-regulation is one possible approach which as been suggested by several legislators, but regulation will do nothing to promote the adoption of new technology. Nor will it promote an abundance of program and service choices for customers. Only market forces will accomplish these vital policy goals; in fact, past experience in other markets suggests that regulation is likely to actively hinder innovation and diversity. We at GTE believe, that regulation is appropriate only where market solutions are not feasible. In the cable TV market, real competition as a policy solution has not yet been tried. Since the problem in the cable industry appears to be the lack of a competitive market, we believe that the introduction of competition is the best remedy.

E. HOW MANY WIRES?

The telco/cable cross-ownership issue is often framed as the question of whether there should be one wire or two serving every home. GTE does not believe that this is the policy issue facing Congress. Today, only one-wire -- controlled by the cable company -- is permitted to supply video to consumers. The issue is whether policy will permit a new entrant, the telephone company, to bring greater competition, greater capabilities and greater choice to this market. Once that decision is made, there is no need to mandate how many wires there will be; the market will make that decision. Several market outcomes are possible, and the result will probably vary from one place to another. However, any of the possible outcomes that will result from adopting our policy recommendation will be better than the current state of affairs.

First, a new national policy which makes entry into video markets feasible for telephone companies will bring a market discipline to cable which does not exist today. Cable operators will have any incentive to improve service and hold down rates to forestall telco entry. This is a benefit which will result immediately if the cross-ownership ban is lifted, before the telephone companies actually install a single broadband line, and will continue indefinitely even in those areas where telcos do not choose to provide broadband service.

Second, with the ability to provide video programming telephone companies will proceed at a more rapid pace to offer broadband service in their areas. This will occur in some areas which are not served by cable today. In those areas, telco entry will provide wider availability of video services to consumers. Telephone companies will also provide video service in areas currently served by cable. In those areas, telco provision of a second, and more capable, wire will provide the benefits of a more open and competitive video marketplace.

Third, in areas served by both cable and telephone systems, the cable company will have a choice: it can continue to maintain and enhance its own system, or it may find it preferable to purchase capacity on the telephone company system. This is a business decision each cable operator will have to make, and it is difficult to predict the outcome. It will depend, in part, on the relative efficiency of the two companies, and on the magnitude of the benefits of integration described earlier in this testimony. The point is that telco entry will open up the market, for consumers and program providers alike, regardless of the choice the cable company makes in a particular serving area. In either event, there will be multiple providers of programming: the cable company, the telephone company, and others, all of whom will be able to buy video transport at the tariffed rate. None of the policies proposed herein would jeopardize the cable company's right to have its own system, nor limit its access to telco poles and conduits for that purpose.

In any of these scenarios, the removal of the cross-ownership ban will provide benefits for consumers. Rather than attempt to second-guess the market or predict the efficiency of future technology, the best policy Congress can follow today is simply to open the market.

F. CONCERNS RAISED BY TELCO ENTRY

As with any controversial public policy question, the entry of telephone companies into video services has generated much discussion. The traditional suppliers of video programming paint only the most lurid canvas imaginable. "Telco TV" has become a pejorative term that implies a multi-headed monster that controls every bit of information available to the public and that dislodges major industries (broadcasting, cable, publishing, program production) on a capricious whim.

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GTE suggests that the marketplace should decide these questions, not the hyperbolic statements of those who fear real competition.

It is then suggested that telephone networks will prevail in the market, not on their own merits, but because they will be subsidized by local telephone rates. Let's examine this proposition for a moment. The basic local telephone rate is actively regulated by state commissions, for whom minimizing this rate is an important public policy goal. The fervent resistance to increases in local telephone rates is illustrated by the controversy generated by federally-mandated subscriber line charges. For example, the recent increase of $.60 in December of 1988 was implemented only after an intense nation-wide debate. How exactly in this closely regulated environment, could telephone companies engineer local rate increases sufficient to subsidize their entry into video markets?

The fact is that cable operators would enter the competition with telephone companies with advantages most competitive firms do not have. They are entrenched incumbents with a monopoly in their current market, but no regulatory constraint on their rates. They have their networks in place, and more than half of the potential subscribers in the country (the more profitable half) already signed up. They have experience in video programming, and ties to programming firms, that telephone companies lack. When we set out to compete with these firms, we in the telephone industry will be taking on formidable opponents, with no assurance of success. It is highly unlikely that either industry will "win" this competition, in the sense of driving out the other firm. Rather, we expect that both of us will remain in the market indefinitely, and as a result of our competition it will be the customer who wins.

Of course this outcome is not attractive to the cable industry. It is competition itself, rather than the mythic specter of "telco TV" that cable operators really fear. It appears that the concerns raised by the cable industry over telephone company provision of video services have more to do with cable's own desire to maintain its protected status than with any real threat to ratepayers or to fair competition.

It is nonetheless understandable that policy makers should wish to condition telco participation in video markets on the existence of safeguards which would prevent any unwarranted discrimination, however unlikely. I will therefore discuss the safeguards which are available to deal with the two main areas where concerns have been raised: access to the network and cross-subsidy.

VII. CONSUMER AND COMPETITIVE SAFEGUARDS

A. ACCESS TO THE NETWORK

Concern that telephone companies could inflict harm on fledgling cable firms by denying them access to facilities motivated the 1970 cross-ownership restrictions. However, much has changed since 1970 to make it difficult if not impossible for a telephone company to deny access to a cable provider. In 1978, section 224 was added to the Cable Act which permits either individual states or the FCC to regulate the terms and conditions of pole attachments. Although the Pole Act does not mandate access to utility poles, GTE believes that the state and federal administration of this law has worked satisfactorily.

More significantly, the FCC's proceedings in establishing Open Network Architecture ("ONA") requirements for the Bell Operating Companies in the Computer III inquiry provides a useful model for how all telephone companies might provide access to their facilities. A telco fiber facility, for example, that could provide both voice and video services could be conditioned with ONA-like restrictions that could define various "levels" of basic and enhanced video services for which the telephone company would be forbidden to favor itself. In its comments last December in the FCC's Notice of Proposed Rulemaking in Docket 87-266, GTE suggested a range of services from basic video transmission to full-blown video program creation, including production and distribution. Assuming some sort of 214 application process remains, the telco's video services could be conditioned with non-discriminatory ONA-like requirements.

It is true that the ONA process for information services is only at its formative stages. GTE is confident that as the telecommunications industry and the FCC becomes more experienced with the needs and requirements of the public that an efficient and effective procedure will emerge. Certainly, the learning curve for ONA application to the video world will be considerably faster once ONA is implemented for today's information services environment. I would like to point out that when we set out to create this ONA environment for video services, we will begin from a starting point that does not exist in the current ONA environment for enhanced services. Under present conditions, the telephone company begins as the incumbent supplier of access to the customer, and other enhanced service providers need access to our network for that purpose. In the video market, we are not the incumbent firm. Cable operators already have wires passing 85% of the homes in America, while the telephone industry has broadband access in few places today. As we expand our broadband capabilities, we will not be, as the cable company is today, the only wire to the home. The ONA framework I have described will guarantee the cable firm access to our network. At the same time, the cable company will retain its own network, and will be able to use whichever access is most advantageous. In this environment, the telephone company simply will not have an opportunity to deny competitors access to subscribers.

B. SAFEGUARDS: CROSS-SUBSIDY

The second major concern that has been raised over telco entry into video markets is that of cross-subsidy. It has been suggested that investment in broadband capability will be recovered from existing POTS ratepayers in such a way as to cross-subsidize telco entry into the CATV business. As outlined earlier in this document, fiber optics is the most efficient and economical transmission medium for voice and data as well as video. The telco networks are using increasing amounts of fiber to provide existing services. GTE will enter the video services market in the expectation that any additional costs to provide video transmission will be supported by video service rates. As I have already explained, given the close oversight of local rates by state regulators, we would be foolish to expect basic telephone rates to support our video business.

Further, state regulation of telephone rates is rapidly evolving toward new models which will eliminate the mechanism through which cross-subsidization is claimed to occur. Under these models, traditional rate of return regulation is supplemented by specific agreements which limit the level of basic service rates. For example, the California PUC recently approved a plan limiting basic rate increases to an inflation index LESS a 4.5% productivity improvement factor. Since these basic rates are controlled directly, they are not dependent on the allocation of costs among different services. Thus any unlikely shifting of allocated costs from CATV services to basic services will not increase basic service rates above the controlled limit. Investigations into alternative regulatory frameworks have been undertaken by more than half of the 50 state commissions, as will as the FCC. Some states, including California, Wisconsin and Missouri have already adopted such plans, and more are expected to do so in the near future.

VIII. CONCLUSION

These hearings are not merely concerned with permitting telephone companies to provide CATV programming in their franchised areas. Opening up the cable market to real competition by allowing telephone companies into the business will have many positive benefits for consumers and the American economy. Competition in an open marketplace will lower cable rates and will provide incentives to competitors to provide the highest quality and most innovative services. Telco competition will not mean simply more movies and sports programming. It will mean a fuller and richer array of video and interactive information services for both residential and business users. Because the telco network will have more capability than today's cable networks, and because this capability will be available to anyone at tariffed rates, telco entry will create a more open market in which many participants can offer new programs and services.

This dynamic market, based on a broadband telecommunications infrastructure, will provide the integrated voice, data and video services that American business will need to compete effectively in the future global economy.

Members of Congress have an opportunity to turn this vision into a reality. Removing the ban on telco programming and making the necessary modifications to current franchise practices will allow the benefits of the information age to accrue to this and succeeding generations.

Senator **Gore**. Thank you very much.

Our final witness is Mr. Dean Swanson, Chair of the United States Telephone Association based here in Washington. We are delighted to have you here. Please proceed, Mr. Swanson.

STATEMENT OF DEAN C. SWANSON, PRESIDENT, STANDARD TELEPHONE CO. AND CHAIRMAN, U. S. TELEPHONE ASSOCIATION

Mr. **Swanson**. Thank you very much, Senator. And in the interest of time, I will abbreviate my remarks this morning.

Mr. Chairman, the most important message I come to share with this committee is unless telcos are freed from anticompetitive restraints, including the Cable Act's cross ownership restrictions, American consumers will be forced to wait for new services made possible by a fiber based broadband network and other advanced network capabilities.

My testimony's silence on the cable problems being experienced in many communities should not be read as being insensitive. That difficulties are being experienced, was documented in yesterday's testimony by representatives of local governments. And I think that message has also been brought home today. But, Mr. Chairman, if calls for reregulation are all that this committee hears and heeds, then I respectfully suggest that these hearings will not be the success they should be.

The telephone industry's vision for cable is one of a diverse and competitive environment that would benefit both the American consumer and American business, a competitive environment that would provide safeguards to the viewing public and enhancements to this Nation's economic strength as measured by its telecommunications infrastructure, an environment that this Congress has the opportunity to hasten by passage of legislation that frees the telephone industry from artificial and unnecessary restraints.

The results of 20 years of a noncompetitive cable market are not only unfettered rate escalation in some communities, but perhaps more tragically that nearly one in every five homes in America still does not have access to cable. While telcos seek the opportunity to offer video entertainment to our customers, that is not our only objective. The industry's concerns are much broader as it looks to chart the future course of telecommunications in this country that will include all, not just four out of five, households.

America's local telephone companies are uniquely capable of providing broadband services at reasonable prices with high customer satisfaction. In fact, over 200 telephone companies currently provide cable to rural areas of less than 2,500 population, areas cable has chosen not to serve due to high capital and maintenance costs. Telephone companies, however, as providers of last resort, serve these communities. As I said earlier, we take our responsibility to serve consumers, wherever they are found, very seriously.

Our opponents say that we cannot afford to rewire America with fiber and offer other emerging technologies. The telephone industry's response is that we cannot afford not to.

According to Bellcore, the costs to rewire America with fiber is likely to be less than $230 billion or a little over $10 billion a year to the year 2012. While this sounds like an extremely large number, the telephone industry already invests over $20 billion a year in construction overlays. If an accelerated program were desirable, we could fiber all of America in just 10 years were we to double our investment in infrastructure costs.

In summary, that an integrated broadband network will become a vital component of this Nation's infrastructure is clear. What is not clear is how soon.

Federal restraints on telephone companies frustrate and delay our building the telecommunication networks of the future. And yet, the information age will not totally arrive until integrated broadband services can be offered to all the citizens of this Nation. We ask only that we be allowed to compete so we can continue to meet the telecommunications needs of our customers.

Thank you for your time, Mr. Chairman.

[The statement follows:]

STATEMENT OF DEAN C. SWANSON ON BEHALF OF STANDARD TELEPHONE CO. AND THE U.S. TELEPHONE ASSOCIATION

Mr. Chairman, members of the committee, my name is Dean Swanson. I am president of Standard Telephone Co., headquartered in Cornelia, GA, and chairman of the U.S. Telephone Association. I appear today on behalf of Standard and the other 1,100 local exchange telephone companies throughout the country.

My testimony is also presented on behalf of the hundreds of millions of customers USTA companies serve, and to whom we have the responsibility of making our network the most advanced and sophisticated in the world.

The local exchange carrier industry takes this responsibility very seriously. We expend $20 billion per year in new and upgraded facilities to fulfill our obligation to meet the ever increasing communication needs of America. A vital part of this process is the deploying of new technologies, and certainly one of the most significant is the deployment of fiber optics.

Mr. Chairman, the most important message I come to share with this committee is unless Telcos are freed from anticompetitive restraints, including the Cable Act's crossownership restrictions, American consumers will be forced to wait for new services made possible by a fiber-based broadband network and other advanced network technologies.

The ability of local exchange carriers to compete in the video programming marketplace is critical to the development of a broadband fiber network and the services it could provide.

My testimony's silence on the cable problems being experienced in many communities should not be read as being insensitive. That difficulties are being experienced was documented in yesterday's testimony by representatives of local government. But, Mr. Chairman, if calls for reregulation are all that this committee hears and heeds, then I respectfully suggest that these hearings will not be the success they should be.

The telephone industry's vision for cable is one of a diverse and competitive environment that would benefit both the American consumer and American business. A competitive environment that would provide safeguards to the viewing public and enhancements to this Nation's economic strength as measured by its telecommunications infrastructure. An environment that this Congress has the opportunity to hasten by passage of legislation that frees the telephone industry from artificial and unnecessary restraints.

The Cable Competition Act, S. 1068, authored by Senators Gore, Gorton, and Ford, in repealing the crossownership ban would:

Curb upward pressure on cable rates by introducing competitive market forces, thus providing consumer safeguards;

Increase the number of telecommunication service available for consumer choice, including new and varied cable viewing options as additional and independent cable providers are able to enter the marketplace;

Provide financial incentives to accelerate the deployment of fiber optic technology coast-to-coast; and

Speed the day when all Americans, in both rural and urban areas, have available to them the benefit of an integrated broadband fiber optic network.

In 1970 and again in 1984, we were told that crossownership bans were imposed because cable, a then fledgling industry, required protection. Circumstances have changed. Cable, now a $14 billion a year industry still seeks protection in the form of a deregulated monopoly, even though more than half the homes in America are cable subscribers.

Franchising authorities such as the U.S. Conference of Mayors and National League of Cities, who participated in the negotiations that led to the 1984 act, as well as the National Conference of Black Mayors, the National Association of Telecommunication Officers and Advisors, and the American Legislative Exchange Councils Communication's Committee, have all called upon Congress to recognize that competition does not exist in today's cable market and that this situation must be changed.

Each of these associations call for competition, they support Telco entry, they, as we, look to Congress to act.

The results of 20 years of a noncompetitive cable market is not only unfettered rate escalation in some communities, but perhaps more tragically that nearly one in every five homes in America still does not have access to cable. While Telcos seek the opportunity to offer video entertainment to our customers, it is not the only objective. The industry's concerns are much broader as it looks to chart the future course of telecommunications in this country that will include all, not four out of five, households.

Cable television will provide the necessary impetus to accelerate the deployment of fiber optic technology into the public switched network. Through a switched fiber optic network, telephone companies would be able to offer community services such as education and self help courses, interactive television, video-on-demand, sports, entertainment, and other consumer oriented services.

The public interest will not be served by precluding my company, or any telephone company, large or small, from offering telephone customers innovative services over the latest telecommunications technology.

America's local telephone companies are uniquely capable of providing broadband services at reasonable prices with high customer satisfaction. In fact, over 200 telephone companies currently provide cable to rural areas of less than 2,500 population areas cable has chosen not to serve due to high capital and maintenance costs. Telephone companies, however, as providers of last resort, serve these communities. As I said earlier, we take our responsibility to serve consumers wherever they are found very seriously.

Our opponents say that we can not afford to rewire America with fiber, and offer other emerging technologies. The telephone industry's position is we can't afford not to.

Estimating the costs of developing electronic technology is difficult. It was not long ago that the most rudimentary of calculators cost in the hundreds of dollars. Today, many calculators with advanced capabilities cost less than $10 to produce.

According to Bellcore, the costs to rewire America with fiber is likely to be less than $230 billion or a little over $10 billion a year by the year 2012. While this sounds like an extremely large number, the telephone industry already invests over $20 billion a year in construction outlays. If an accelerated program were desirable, we could fiber all of America in just 10 years were we to double our investment in infrastructure costs.

In addition to offering improved service generally, multiple services will be cheaper. For the pricing out of transmissions over fiber, like with any infrastructure service, will be determined by dividing fixed costs by the number of uses on the system. The number of uses for copper are limited, the number of uses for fiber are not. As additional services are developed and deployed, the cost for each service will be reduced accordingly. So despite what others may claim, Telcos being permitted to provide more than just "plain old telephone service" will in the long run result in lower costs for basic telephone service, not higher.

Finally, on the subject of cost, Mr. Chairman, where would this nation be today had Congress decided in 1958 that the building of an interstate highway system was too expensive. For much like the discussions on the interstate, the question was not whether we could afford to build, but whether we could afford not to?

As the cost of fiber optics continues to decrease, the network of choice will include more and more fiber. This network will have the capability to:

Bring a wide array of information and data services to both home and businesses;

Balance and reduce the individual costs of these services;

Make these new services, including cable television, available to the largest possible universe of consumers, including those in rural America;

Serve as an alternative and competitive video programming delivery system for numerous programmers and users; and

Provide third parties, in a user friendly way, with the ability to deliver video, enhanced data bases, shopping and banking at home, computer storage, movies, sports, video information retrieval, and local community programming.

In summary, that an integrated broadband network will become a vital component of this Nation's infrastructure is clear. What is not clear, is "how soon?"

Federal restraints on telephone companies frustrate and delay our building the telecommunication networks of the future.

And yet, the information age will not truly arrive until broadband services can be offered to all the citizens of this Nation. We only ask that we be allowed to compete, so we can continue to meet the telecommunications needs of our customers.

Thank you.

Senator GORE. Thank you very much. I want to tell you the subcommittee appreciates both statements very much.

Let me ask you both this question. Yesterday Mr. Mooney and Mr. Malone claimed that the idea of a single fiber line into the home with data voice and broadband video on that one line is technically infeasible and economically inefficient. Would you comment on their statements?

Mr. FOSTER. We are going to demonstrate in Cerritos, California that it is technically possible and it is cost effective. That is the reason we are putting that experiment in place. This is a community of 6,000 customers. So, it is not a small experiment. And we are doing this at our shareholders' expense. Not a penny of this money is going in under regulation.

Senator GORE. Could you do it in my home town on that basis?

Mr. FOSTER. We could have.

Senator GORE. I'm kidding you. Go ahead.

Mr. FOSTER. But we're not allowed to experiment like this without the approval of the FCC and to convince them to let us proceed, we took all the cost to build the line. This is a very expensive undertaking, but we want to demonstrate to the American public what the telephone companies can do. We have had many visits out there by Members of Congress, staffs, regulators, and they have been very impressed. And our demonstration in Boston at the NARUC convention of our video switch was very well attended. I think people are now beginning to recognize that if we unleash the telephone companies, we can significantly alter the value provided by the communications infrastructure.

We are going to demonstrate it is technically feasible. But if it is not, what are they worried about? What is the concern? Either we can and they have real competitors, or we can't and we are going to drop out of the business.

Senator GORE. Mr. Swanson?

Mr. SWANSON. I think if the telephone companies were freed, Senator, you would see three scenarios develop. In sparsely populated rural areas, you could only afford to have a single fiber to the home. And in those cases as an industry, we are suggesting that there should be regulation of the basic services.

In some areas you would see over time that the telephone companies would become the conduit, the transport vehicle and would strike a deal with the cable people. In other cases, however, including urban areas with which I am personally familiar, I believe you can very easily run two fibers to the home and that they both can be viable.

Senator **Gore**. As for the argument that it is not cost effective, I have information from Corning Glass which indicates that there will be as much as an 80 percent reduction from the current $5,000 to $7,000 per home that it now costs over the next decade, and this as a result of the learning curve, volume production as well as technological advances.

If there was an 80 percent reduction, would that bring the cost of fiber to the home down to nearly the level of copper wire?

Mr. **Foster**. Yes, it would, Senator. I think an important point here is no one envisions out two decades from now us not having a broadband fiber optic based network in this Nation that is integrated so that everyone can call everybody else. I don't think anybody denies that. So, we have to get on to building that, and we ought to be allowed to transport services over that network to help make it happen. Certainly other countries in the world are doing this right now.

If there is only going to be one wire in the home, I don't think it will be a lot of fragmented coaxial networks. That certainly won't carry our infrastructure needs over the next couple of decades.

And our network is open to everyone. Anyone can market their video programming, any other programming, over that network. Just by authorizing us to proceed, it will start igniting sparks of creativity in people who want to design new computers, new data bases, new sources. And that network is open to all.

The CATV networks are controlled by a single company. They are not interconnected. You can't call from one to the other. So, the 1984 Cable Act has resulted in a lot of investment going into networks, and the American public is paying for all these networks. But it has resulted in them going to networks that are not really functionally effective. So, I don't see how we can have anything other than a broadband public switched network.

Senator **Gore**. Well, now, the cable industry and some others in this debate have expressed the concern that there simply is no way to develop adequate protections against the kind of cross subsidies that are feared if telephone companies get into this business and no effective way to prevent unfair behavior against existing competitors.

Mr. Swanson, I understand that several hundred smaller telephone systems throughout the country already provide cable services under state regulation prohibiting cross subsidies. Is that correct?

Mr. **Swanson**. That is correct, sir, over 200.

Senator **Gore**. Well, do they work in your opinion?

Mr. **Swanson**. They are not only working, they are working very well, particularly from a small company standpoint.

We are audited in a number of different ways, but our real auditing concern comes from the state regulatory authorities. They show up frequently and unexpected. In fact, our company has just gone through such an audit. They spend two or three weeks with our company with a complete audit team going over all of our books.

We have examples of companies providing inside wiring and customer premises equipment on a deregulated basis. The regulators are very well aware of that, and they are looking very closely to be sure there is no cross subsidies.

Senator GORE. Do you believe the FCC could produce similar protections against cross subsidies by larger telephone companies?

Mr. SWANSON. At the present time, the FCC in general develops the accounting rules and regulations that we all use even at the state level. So, once those rules are established, even if a state auditing team came in, they would be using the rules that were established to prevent cross subsidies by the FCC. But the enforcement procedure, even with larger companies, would most likely be the responsibility of state commissions, and certainly they could do the job.

Senator GORE. Mr. Foster, I am sure you would like to address this question.

Mr. FOSTER. The large companies have auditors living in their buildings around the clock.

Senator GORE. Is that an argument for it or against it?

Mr. FOSTER. Just to point out that our state regulators take their job very, very seriously and are constantly on guard to ensure that the ratepayers are not cross subsidizing unregulated services. And they will have to do that whether we are in this business or not.

But let me just say we are proposing a pipeline that is provided by telephone companies under regulation, and that pipeline will be available to all under tariff. If we are allowed in the programming business, it will be an unregulated subsidiary who buys at the same price, terms and conditions. That is very easy to audit, and it is also available to anyone. Unlike reregulating CATV, which means you still only have one source, we will open up a pipeline to anyone and everybody has the same shot at it.

Senator GORE. Well, let me say in concluding these hearings that I am particularly grateful to the two of you for coming at the end of the hearing.

And I wish to again express thanks to Chairman Inouye for his decision to schedule these hearings. In a letter to members of the subcommittee, he has expressed his intention to proceed in the deliberate, careful fashion that was referred to by Senator Danforth yesterday. We will probably be engaged in continuing discussions with all participants in this controversy in an effort to come up with a bill that can have widespread support and then in the new year move toward action on that legislation.

I am encouraged as one who has been in the trenches for quite a number of years on this issue. I am very encouraged at the new willingness of participants within the industry to participate in a meaningful dialogue and the growing support within the Congress and particularly the Senate for legislation to address the problems we have discussed for these two days.

With that and with a word of thanks to all of the witnesses on both days, we will have these hearings adjourned.

[Whereupon, at 1:33 p.m., the subcommittee was adjourned.]

ADDITIONAL ARTICLES, LETTERS, AND STATEMENTS

STATEMENT OF GENERAL INSTRUMENT CORPORATION VIDEOCIPHER® DIVISION

General Instrument Corporation (GIC) is pleased to submit this statement for the record in the Committee's November 16 and 17, 1989 oversight hearings on cable television.

Although home satellite television issues received minimal attention at the hearings, such discussion as did occur focused primarily on erroneous and misleading statements, reflecting misconceptions about the state of the satellite equipment market. We submit this statement for the purpose of correcting the record, as well as to report on the status of the home satellite television industry, on the progress which has been made since the last Senate hearings on this subject, and on other issues of importance, particularly as they affect the VideoCipher system and equipment.

CORECTING THE RECORD

The erroneous and misleading statements, and our summary responses, are listed here. More extensive background on these issues can, where appropriate, be found later in this statement.

ERRONEOUS STATEMENT

GIC has stopped manufacturing standalone decoders, forcing consumers to buy integrated receiver descramblers that contain unneeded features.

RESPONSE

GIC has not stopped manufacturing standalone descramblers. VC II standalone descramblers are available now, and VC II Plus standalone descramblers will soon be available. However, the demand for standalone descramblers has continued to decline over the last three years. The largest marketplace demand now is for integrated receiver descramblers ("IRDs") which have met with widespread consumer acceptance. (IRDs are manufactured by General Instrument Corporation and by twenty-one other licensees of the VideoCipher technology.) As a result of this shift in demand to IRDs, there are more standalone decoders available today than there are buyers for them. It is true that, particularly with respect to earlier models, a price premium exists in the pirate marketplace because they are perceived as more easily modified to permit theft of signal.

ERRONEOUS STATEMENT

GIC manufacturers its VideoCipher descramblers in Taiwan, a foreign country.

RESPONSE

VideoCipher descramblers are manufactured in Puerto Rico, a United States territory. Research & development and engineering is done in San Diego, California. Repair and warranty work is done primarily in Hickory, North Carolina.

FALSE STATEMENT

Mandatory decoder standards will solve the piracy problem and bring lower decoder prices.

RESPONSE

A mandatory decoder standard would cause public confusion and uncertainty during the 2-3 year FCC proceeding leading to a standard; it would decrease system security by making public the details of the scrambling system; it might permit foreign manufacturers to dominate this product sector; and, depending on the details of the standard that is chosen, is as likely to cause decoder price increases as decreases.

In a current FCC proceeding on standardization, not one major organization, group or corporation supported such standards. The only support for such standards came from Chuck Dawson, who reiterated that support when he appeared as a witness at the Senate Hearings on November 17, 1989. Before Mr. Dawson's request for standardization should be given any consideration by the Congress, he should be asked to articulate how standards would benefit consumers or the industry and to explain why, when offered an opportunity to provide such information to the Commission in a proceeding mandated by the Congress, he failed to do so. Mr. Dawson failed to respond to the Commission's Notice of Inquiry and request for information other than to file an audio tape of a call-in satellite radio program. No attempt was made by Mr. Dawson or his audience (nor did Mr. Dawson encourage his audience) to address any of the issues and questions raised as part of the Commission proceeding. Yet he is now before the Congress repeating his demand for standardization without providing any explanation of how it would work or how consumers would benefit.

THE HOME DISH INDUSTRY IS HEALTHY AND HAS MADE GREAT PROGRESS IN THREE YEARS

The home dish industry is more healthy than it has been in several years. Dish sales have been strong this summer and fall. Descrambler authorizations have run at near record levels for the past three months. Churn has decreased. There appears to be a significant inventory buildup by distributors and receiver manufacturers, in anticipation of even stronger sales ahead. The progress in the last three years has been substantial.

There are currently some 617,000 authorized descramblers in use. Three years ago, in October 1986, the number of authorized descramblers were 43,500.

Including pay-per-view services and regional sports networks, there are now 39 programmers scrambling with the VC II system. In October 1986, there were nine programmers using the VC II system. Programmers are realizing approximately $12 million per month in home dish revenues, and this is growing at about 6% per month.

In October 1986, General Instrument had licensed seven receiver manufacturers to incorporate the VideoCipher II scrambling technology into their integrated receiver descramblers. There are now twenty-one manufacturers building these IRDs. The IRD industry is highly competitive and manufacturers have introduced receivers with a wide range of features and prices.

At this time, about 50% of the descrambler modules used in these IRDs are manufactured by GIC, and about 50% are manufactured by Channel Master (a division of Avnet, Inc.), a second source licensee of the modules. During some months, Channel Master has supplied as much as 70% of the demand for modules.

Commercial descramblers, used in cable TV headends, SMATV operations and other commercial establishments, are also supplied in a competitive marketplace. There are currently eight licensees of commercial descramblers.

These rank as additional positive factors in this industry:

the successful installation of over 128 scramblers at programmer uplink facilities;

the installation of over 206,000 commercial descramblers;

the improvement in picture quality for home satellite subscribers;

introduction of compact disk quality digital audio;

the broad development of program packages and increased ease of customer ordering;

the introduction of pay-per-view services; and

the offering of ancillary data services for the home dish market.

THE VIDEOCIPHER II PLUS HAS BEEN INTRODUCED AS A RESPONSE TO PIRACY

Piracy remains the major problem facing the home dish industry. The VC II has been the target of well-financed international cartels whose sole purpose is to break the security features of the system and then merchandise signal theft devices as widely as possible.

As one of several responses to piracy, GIC is in the process of introducing the VC II Plus system. The VC II Plus system is designed to offer advanced system security as well as additional capacity to address home satellite TV subscribers and expanded channel capacity for programming delivery. It is based on a three year R&D program costing $30 million.

A number of significant milestones for the introduction of the VC II Plus have passed. On May 16, 1989, a beta test VC II Plus uplink was installed at one programmer's location. It has been operating since that time in a manner compatible with VC II descramblers. One month later, a second channel was upgraded to VC II Plus. In late May, a meeting was held in San Diego for programmers' technical staff for hands-on work with software to be installed at their uplinks. A second meeting was held in November. In early June, there were field tests at additional programmers' locations. A full-scale rollout at uplink sites began July 31.

Field tests of prototype descrambler modules were successfully tested for authorization, over uplinks that had been upgraded to VC II Plus, in July. By late August, some 100 prototype descramblers were being tested.

All licensed manufacturers of integrated receiver-descramblers have received the new VC II Plus system specifications and we believe they are preparing their production lines for VC II Plus integration later this year.

The initial production of VC II Plus modules began September 28, 1989. Fifty-five uplink sites have now been installed. Two hundred twenty VC II Plus consumer descramblers are now being used in active field tests. At the earliest possible date, we plan to move to 100% production of VideoCipher II Plus modules, discontinuing the VideoCipher II module.

THERE IS NO NEED FOR TODAY'S SUBSCRIBERS TO UPGRADE TO THE VC II PLUS

The VC II Plus system is backward compatible with VC II descramblers currently in use. This means that current VC II subscribers can continue to receive the programming that they currently receive without any change in equipment. Nevertheless, some self-styled "spokesmen" for satellite consumers are attempting to scare those consumers into believing that their equipment will have to be replaced. Such irresponsible behavior is damaging to consumers, to satellite dealers and distributors, to manufacturers and to programmers.

We do not have any plan for mandatory replacement of legally authorized VC II descramblers at this time. Since the existing unmodified VC IIs are being used by legitimate subscribers, who regularly pay their monthly subscription fees to the programmers, there is no plan to replace these units with VC II Plus units. Although these units are vulnerable to piracy, their owners have shown that they reject the piracy approach. Moreover, there is now a population of about 200,000 commercial VC II descramblers. We expect that there will be a significant population of VC II decoders for many years.

We have announced a voluntary upgrade program for consumers who want to make use of the enhanced graphics, additional channel capacity and data channel features. Beginning April 1, 1990, legitimate VC II descrambler or IRD owners, distributors and dealers can trade in unmodified and undamaged VC II modules for a VC II Plus module for $129 (plus shipping and handling). But we stress that this upgrade program is totally voluntary. No VC II subscriber need upgrade to the VC II Plus in order to continue to have access to currently scrambled programming.

AN FCC-ADOPTED MANDATORY DECODER STANDARD WILL NOT SOLVE THE PIRACY PROBLEM

Adoption of a published encryption standard is likely to increase, rather than decrease, the incidence of piracy. An open FCC rulemaking proceeding and the existence of a public encryption standard will not improve the security of a system. On the contrary, they will only degrade security by opening a process that should be closed, disclosing sensitive information and limiting the ability to use electronic countermeasures.

Security systems should not be designed or adopted in an open, public environment. An FCC rulemaking proceeding, which must be open to the public, might allow sophisticated pirate manufacturers the opportunity to influence the security of the standard that is adopted. They could, for example, participate in the proceeding appearing to be legitimate parties, and suggest system design criteria that later turned out to be "Trojan horses" leading to lower security.

A MANDATORY DECODER STANDARD WILL NOT RESULT IN LOWER DECODER PRICES

Adoption of a scrambling standard might have an impact on descrambler prices, but it is as likely to cause price increases as price decreases. It all depends on the details, features and capabilities of the chosen standard. As the record in FCC Docket No. 89-78 shows, an FCC standards decision could well favor a "Cadillac" encryption system with vast (possibly unwanted) capabilities using the latest in technology that turns out to be very, very expensive. The FCC does not have expertise or manpower in encryption technology, has no basis for choosing among competing criteria for an encryption system, and could make a decision that imposes unnecessary costs on the public.

In addition, the contention that standardization would decrease prices rests on the faulty premise that a standard would increase competition in manufacturing. In fact, the home dish marketplace is relatively small, far smaller than the home TV or VCR market, and cannot be expected to exhibit the economies of scale that have resulted in lower costs for those products. While average prices for descrambling capability have decreased over the last three years (as the market has moved to lower priced modules at $150 to $180 and away from standalone descramblers at $395), increased costs for the greater security of the VC II Plus module will be felt by future consumers. The lesson for standardization is that increasing security increases cost.

AN HDTV-COMPATIBLE ENCRYPTION FORMAT IS PREMATURE

At the November 17 hearing, Chuck Dawson testified that a new encryption system should be designed to be compatible with HDTV. Such a suggestion is premature at best, and has the effect of causing uncertainty and confusion in the home satellite dish marketplace.

The FCC Advisory Committee on Advanced Television has recently scheduled tests of proponent HDTV formats for television broadcasting; these tests run until late 1991. It is unlikely that the FCC would make a decision on an HDTV format until late 1992. HDTV broadcasting will probably not begin for at least two years after that decision, in late 1994, because it will take at least that long for transmitting and receiving equipment to reach the market. It is reasonable to estimate that satellite HDTV broadcasting might also start at about that time.

No home dish programmer has proposed to start distributing an HDTV signal. There is no Government or industry organization that is working to develop or adopt a satellite HDTV standard format. Until a standard format is developed, it would be futile to decide on an encryption approach that is HDTV-compatible.

Mr. Dawson's proposal does little more than confuse some home dish customers by making them think that satellite HDTV is coming in the next year or two. That simply is not the case.

CONCLUSION

In 1988, Congress passed the Home Viewer Satellite Act which addressed the two most important issues faced by the industry: 1) the need to provide compensation to producers of programming so that it could continue to be available to consumers; and 2) the need for stricter and more effective penalties for satellite signal theft. These measures have made 1989 the best year in recent memory for the home satellite television industry and its customers.

As the industry continues to develop, General Instrument Corporation, in recognition of its important role in home satellite television, welcomes continued Congressional oversight and pledges its continued cooperation in supplying information and data to the Congress.

Joe Windish
147 West 95th St.
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1989 OCT 30 AM 11:41

24 October 1898

The Honorable Ernest Hollings
U.S. Senate
Washington, D.C. 20510

Dear Senator Hollings:

I understand Congress will be reviewing the effects of the Cable Communications Policy Act of 1984. As the director of a Public Access Television Center in suburban New York City, I have seen community television work well. But I am concerned for its future. The access provisions of the Cable Act are important and need to be improved.

The community I work in (Larchmont and Mamaroneck, New York) is dominated by television from New York City. There is barely any coverage of local politics, schools, sports or people on local television. There is no local newspaper. The Gannett Newspaper serving our area is a regional, so again there is very little coverage of local happenings. But it is not merely that our channels provide the community with local information. We provide more. We provide a great deal of the shared experience that is necessary for a sense of community to exist. The volunteer community producers of Larchmont - Mamaroneck Community Television (LMC-TV) are at almost every fair, festival, debate, community meeting, or school event in our area.

But I am writing today for those areas that are not as fortunate as the one I work in. Larchmont and Mamaroneck were aggressive early on when cable came to their area. Many of the surrounding communities were not and are now struggling to get access television up and running. Manhattan, my home, has a very feeble access arrangement and is in the process of renegotiation. Cable television can, through public access, play a major role in keeping individuals aware and involved in the communities they live in.

It is vital that we strengthen and support access. The Cable Act should be modified to ensure that access is available in all communities and that communities can insist that cable operators support access operations at levels adequate to meet community needs. I would appreciate it if you would please keep me informed of your efforts in this area. I look forward to being in touch with you in the coming months as you consider these issues. Thank you for your time and consideration.

Yours sincerely,

Joe Windish

DANIELS
&ASSOCIATES

Bill Daniels

November 6, 1989

Honorable Ernest F. Hollings
Senate Committee on Commerce, Science and Transportation
SR-125 Russell Senate Office Building
Washington DC 20510-4002

Dear Senator Hollings:

In view of the upcoming Senate Antitrust Subcommittee hearing to weigh the competitive consequences of cable television sports programming, I submit the attached research study for the record.

The study shows beyond question that Prime's affiliated regional sports networks are serving the public interest with no measurable adverse consequences for American television viewers.

As the attached independent study shows: a) Prime Network and its affiliated regional sports networks have not adversely affected the amount of sports programming on broadcast television, b) Prime Network and its regionals have substantially increased the amount of sports programming on television generally, c) Prime Network and its regionals have given television viewers much greater diversity in sports programming, and d) Prime network and its regionals have brought to television several sports and sporting events that had not previously been televised.

Prime Network and our affiliates have given the American television viewer more sports, more choice and more teams without taking away from broadcast television the events that traditionally have appeared on that medium. For the athletes, teams, universities and local advertisers, there is a new-found access to television. For professional and collegiate entities, there is a new-found source of revenue to ensure their sports' continued survival. All of this is the result of cable television and the free market system.

I find deplorable the effort by a small fraction of the broadcast community to use the Congressional process to limit the number of bidders competing for sports programming. This kind of tinkering with the free market system almost always fails, but often with enormous, adverse, short term consequences for the consumer.

I am confident that you and your committee will scrutinize closely the claims of those broadcasters whose motives are the protection of their own competitive position rather than the viewing interests of the American public.

Respectfully,

Bill Daniels

Enclosure.1/

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1/ The enclosure was not reproducible.

CINCINNATI COMMUNITY VIDEO

November 14, 1989

NOV 17 [illegible] 6:2

The Honorable Ernst Hollings
United States Senate Senate Office Bld.
Washington, DC 20515

Dear Senator Hollings:

Localism and diversity in media which Congress has promoted for 50 years could be at stake without your help in fostering input from the users of public access programming.

This fall, as you hold oversight hearings on the cable industry, we urge you, as a member of the Senate Communications Subcommittee, to request testimony be heard from the representatives of the millions of people across the country who, despite the problems with the Cable Act are producing and viewing over 10,000 hours per week of original community programming.

Public access, as you may know, is citizen-produced cable television. In Cincinnati it provides a video reflection of our town ranging from Cincinnati Public School's "Bicentennial Chorus" to the Museum of Natural History's "Dinamation." It carries programming produced by the agencies of United Way such as the Better Housing League and Cancer Family Care to both small and large arts institutions, senior citizen centers and the disabled community.

As a community access center in Cincinnati we have very specific concerns with the 1984 Cable Communications Policy Act. These are:

1) Access channels are not mandated and can be dropped if local politicians decide they need to be. Access channels need to be mandated.

2) Funding for access by the cable operator in addition to franchise fees is not required at renewal time. This means that in 7 years when Warner Cable wants to continue to provide cable in Cincinnati, they may not fund access. Operational funding for access needs to be provided.

3) Cities and access centers need to be clearly exempted from content liability for access programs just like cable companies.

Congress' vision of access fostering a "wide diversity of information sources for the public," which Congress recognized is "the fundamental goal of the First Amendment," can be realized for all Americans through public access. It is virtually the only accessible video resource available in which citizens can control and direct.

We look forward to hearing about your position on this matter and trust you will keep us informed of any developments in Congress that might affect these priorities.

Sincerely,

Joyce Miller

Joyce Miller
Executive Director
Cincinnati Community Video

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1989 NOV 17 PM 2: 1

November 15, 1989

Honorable Ernest F. Hollings
Chairman, Committee on Commerce,
Science, and Transportation
United States Senate
Washington, D. C. 20510

Dear Mr Chairman

I understand that the Mayor of Bayonne, New Jersey is scheduled to appear before the Communications Subcommittee tomorrow as part of your hearings on cable regulation.

The dispute between Bayonne and Cablevision over the loss of the Madison Square Garden Network programming prompted some strong emotions, and I suspect that some of those emotions may spill over into the hearing later this week. On behalf of Cablevision, I thought it would be helpful to you to have the facts surrounding the Bayonne matter.

Pleased don't hesitate to contact me if I can be of further assistance.

Sincerely,

Charlie

Charles D. Ferris

CDF:dls

Enclosure

9247f

The Facts About Bayonne

When all the rhetoric is stripped away, the city of Bayonne's decision on June 15, 1989, to deny Cablevision's renewal application was the result of Cablevision's contractual dispute with the Madison Square Garden Network (MSG) and its temporary loss of the right to transmit MSG, a sports programming network.

Federal and State Law Bar Bayonne From Denying the Franchise Renewal on the Basis of a Programming Dispute. Cablevision temporarily lost its rights to transmit MSG when it refused to accept new contract provisions which would have forced Cablevision to pass the costs of MSG's contract with the Yankees through to all of its Bayonne subscribers. The result would have been higher basic service rates for everyone -- even those customers with no interest in MSG's programming. Cablevision has since satisfactorily resolved its dispute with MSG and regained the right to carry its programming.

Cablevision understands and regrets that the temporary loss of the MSG programming may have been frustrating to many of its customers in Bayonne. But the city's decision violates the fundamental provisions of the Cable Act and New Jersey law prohibiting franchising authorities from denying renewal because an operator chooses to carry (or not carry) particular programming services. Those provisions protect First Amendment rights by preventing the government from using its power to influence the specific programming content of a cable system. The city's own franchise advisory committee recognized that the law prevents denial of a franchise over a dispute about programming.

Cablevision Has Earned Renewal. Since 1979, when the franchise was first granted, Cablevision has added 24 new cable services to its programming menu. It is now offering to expand and upgrade the system from 39 to 50 channels. Cablevision of Bayonne has historically had one of the lowest levels of complaints to New Jersey's Office of Cable Television, and, in a recent survey, Bayonne subscribers expressed satisfaction with the service provided by Cablevision.

Under New Jersey law, the authority to award cable franchises and grant renewals is vested in the New Jersey Board of Public Utilities (BPU). The city's decision to deny Cablevision's renewal application is really a recommendation to the BPU. Cablevision has petitioned the BPU to set aside the city's recommendation and to grant the renewal application. That petition is currently pending.

6760c

— CBA — COMMUNITY BROADCASTERS ASSOCIATION

November 16, 1989

BY HAND DELIVERY

Senator Daniel K. Inouye
Chairman, Communications Subcommittee
Room SD-508, Dirksen Senate Office Building
Washington, D.C. 20510-6125

Dear Senator Inouye:

I am grateful for the opportunity you provided to the Community Broadcasters Association to testify at the hearings on cable television carriage of broadcast signals held on October 25, 1989.

At the hearing, you announced that the record would be kept open until November 16, 1989, for the receipt of additional written testimony. In response to your invitation, I am enclosing letters from low power television stations indicating the serious problems these operators have experienced in trying to secure cable carriage:

1) Rural Television Systems has been thwarted in its attempt to extend national public television service and to introduce local service to rural areas that are not served by any conventional PBS or locally originating station.

2) Warner Cable demanded $500 - 600 per month to carry an LPTV station in Olean, New York, and then declined to extend carriage to Bradford, Pennsylvania, despite subscriber demand for the service.

3) A cable system serving Rhode Island and neighboring Massachusetts communities has refused to carry a new LPTV station, even though it has 52-channel capacity.

4) Cable systems in Montana encourage their customers to claim an exemption from local taxes used to support over-the-air TV service via translators, even though those subscribers may also have outdoor antennas. The cable systems successfully lobbied to defeat legislation designed to close this loophole and to preserve funding for over-the-air service.

5) In Raleigh, North Carolina, an LPTV station continues to be bounced back and forth between cable officials and city officials and cannot get a firm decision on whether or not its signal will ever be carried on cable.

P.O. Box 26736 • Milwaukee, WI 53226 • (414) 783-5977

Senator Daniel K. Inouye
November 16, 1989
Page 2

6) A community station serving Wailuku, Maui, Hawaii was denied carriage on the local cable system despite the fact that this LPTV was the first television station in the community and that it was used frequently by Maui's Mayor Tavares as a direct outlet to the people.

7) In Paducah, Kentucky, denial of access to the cable system has caused the demise of the only independent community station and the loss of ten jobs. In the meantime, the system, Comcast cable, allots two channels for the local full power NBC affiliate.

Thank you again for your time and concern.

Respectfully yours,

John Kompas

John G. Kompas
President

JGK/cc

Enclosures. 1/

1/ The enclosures were not reproducible.

PRIME
TIME
24

342 Madison Avenue Suite 1520 New York, NY 10173
(212) 599-4440 Fax: (212) 599-2402

November 17, 1989

Senator Daniel K. Inouye
Chairman, Senate Communications Subcommittee
Room 227 -- Hart Senate Office Building
Washington, D.C. 20510-6130

Dear Senator Inouye:

As you and your colleagues evaluate the need for cable reform legislation, we would like to draw your attention to the pending acquisition by Tele-Communications Inc. (TCI) of a 50% ownership interest in Showtime Networks Inc. (Showtime) and its subsidiary Showtime Satellite Networks, Inc.

This proposed sale will create a monopoly in the already highly concentrated business of distributing satellite programming to home satellite dish customers. It is a timely example of monopolistic practices that will further compromise the development of an independent satellite dish industry and will have far-reaching consequences for the competitive distribution of television services throughout the United States.

As the enclosed chart demonstrates, TCI and Showtime are already dominant as packagers of satellite programming. Their combined packaging businesses will, in fact, control more than 60% of the existing market for sales of programming packages. Moreover, TCI's and Showtime's exclusive control of significant channels represents a substantial barrier to entry in the marketplace, now and for the future. Popular channels such as MTV, VH-1, Showtime, The Movie Channel, and Viewer's Choice are owned and operated by Showtime and are not made available to any packagers. Nickelodeon is made available to the National Rural Telecommunications Cooperative on a limited basis. There are also restrictions on the availability of ESPN, WTBS, American Movie Classics, Bravo, and TNT. It is worth noting TCI is a part owner of many of these services, and as a cable operator, TCI is the largest customer for every satellite-delivered cable channel.

The home satellite dish consumer has demonstrated his or her preference for buying programming packages, rather than individual channels. However, the consumer's choice of programming packages will be reduced by this sale. Without access to popular programs at reasonable prices, the success of any packager will be limited, and the number of packagers in the marketplace will decline precipitously.

Home satellite dish technology has offered consumers, particularly in rural areas, greatly expanded entertainment and information options. But now, the largest cable operator, TCI, has demonstrated its intent to control more than 50% of programming sales through home satellite dish distribution, plus limiting access to many of the most important television services.

The control of cable's competition by the largest cable operator defeats the goal of fostering competition and diversity of programming for all Americans.

We urge you to consider enactment of legislation that will ensure the competitive delivery of television programming throughout the United States.

Thank you for your consideration.

Sincerely yours,

Kazie Metzger

Kazie Metzger
President
PrimeTime 24

The Home Satellite Dish Programming Marketplace

Background

There are approximately 2.2 million home satellite dishes in the United States, of which approximately 595,000 are equipped with the legal descramblers that are required to purchase programming. Approximately 464,000 consumers have purchased programming packages.

.Showtime currently sells to approximately 140,000 of these home dish owners as a packager of programming services. Not unlike a cable system, Showtime purchases programming on a wholesale basis from a variety of programmers and markets them together with programming produced by Showtime and its wholly owned companies, the MTV Networks.

.TCI, through its Netlink and Tempo subsidiaries, sells to approximately 145,000 customers. TCI also packages programming from a variety of sources, including programming that it owns all or in part such as the Denver 5 superstations, WTBS, CNN, Headline News, American Movie Classics, and The Discovery Channel.

While there is some overlap of customers, the combined companies will control 50% of the entire market for programming sales today, or 61% of the existing programming package customers.

Packager	Current Authorized Subscribers	Share
TCI's Netlink/Tempo	145,000	31%
Showtime	140,000	30%
Home Box Office	60,000	13%
NRTC	40,000	9%
SuperStar Connection	30,000	6%
Disney	7,000	2%
Turner	2,000	<1%
Other Cable Operators	20,000	4%
Other Distributors	20,000	4%
TOTAL	464,000	99%

Source: Satellite Business News

STATE OF NEW YORK
EXECUTIVE DEPARTMENT
STATE CONSUMER PROTECTION BOARD
99 WASHINGTON AVENUE, ALBANY, NEW YORK 12210

RICHARD M. KESSEL
CHAIR AND EXECUTIVE DIRECTOR

UTILITY INTERVENOR UNIT
(518) 474-5015

November 21, 1989

Toni Cook, Esq.
Counsel
Senate Commerce Committee
Room 227
Hart Office Building
Washington, DC 20510

Dear Ms. Cook:

I regret that Richard M. Kessel, the Executive Director of the New York State Consumer Protection Board, was unable to testify at the November 16, 1989 hearing of the Senate Commerce Committee due to an unresolvable scheduling conflict. We appreciate the invitation and would very much like to be considered for future appearances.

In lieu of Mr. Kessel's testimony, we respectfully ask the Committee to consider the proposals contained in Mr. Kessel's June 8, 1989 letter to Congressman Markey, three copies of which are enclosed.

Very truly yours,

Philip S. Shapiro

Philip S. Shapiro
Intervenor Attorney

Enclosure 1/

1/ The enclosure was not reproducible.

SCCTA

South Carolina Cable Television Association

6175 Barfield Road • Suite 220 • Atlanta, Georgia 30328 • (404) 252-2454

DEC 13 AM 12:11

December 4, 1989

Honorable Ernest F. Hollings, Chairman
Committee on Commerce, Science and Transportation
United States Senate
Washington, DC 20510-6125

Dear Senator Hollings:

Recently, you requested of several South Carolina cable operators some general statistics covering our industry. Specifically, you expressed interest in subscription costs in South Carolina and the handling of service items within our systems. We hope the following information will be useful to you.

CUSTOMER SERVICE

As you know, improving customer service is one of our industry's top priorities. As a relatively new, and still developing industry, we know we must work hard to build a reputation for responsiveness and service. Although in many cases the handling of phone calls - how they are answered and how quickly - are subjective matters, we have managed to generate some statewide statistics which may be of interest to you.

On the average, South Carolina cable systems maintain one incoming phone line per 2,750 subscribers. Of the incoming calls, less than 30% go on hold; and, those calls are answered within an average of 62 seconds. Of all incoming calls, some 30% involve some type of repair. Statewide, those repairs are completed within an average of 24 hours or less. Of course, these figures make no distinction between large and small repairs and are not adjusted for weather or external causes. We view these factors as just the challenges of doing business. Hugo was as devastating to our cable systems as it was to everything in its path. Although cable television is a low priority to a family without a home, it is a factor in a true return to normalcy. We believe that our South Carolina industry has affected repair with a speed and scope unprecedented in the industry nationwide.

The other service area that is of importance is the length of time to complete an installation once the customer places an order. The average completion time in South Carolina is 4.2 days.

SUBSCRIBER RATE INFORMATION

You also requested subscriber rate information for South Carolina similar to the national averages set forward in the GAO report. Short of having the GAO's

--Continued--

raw data, the best data available to us runs through the end of 1988, and generates averages which are very close to the national norms. The average basic cable rate in South Carolina is $14.66 per month, and the average total monthly bill is $23.02 (both somewhat below the GAO's national figure). In addition, the average system in South Carolina provides between 28 and 29 channels of basic service.

We expect to have fresh data shortly after the first of the year and will be happy to provide your office with any information you would like to have. Please, of course, feel free to call on us any time we can provide assistance or answer any questions for you.

We, as an industry in the State, are very proud of the service we provide to our fellow South Carolinians. Our service represents an outstanding value, and we are working constantly to increase and improve that service.

Sincerely,

Nancy Horne

Nancy Horne
Executive Director

NH:ms

GTE

GTE Telephone Operations

Williams Square · West Tower
5205 N. O'Connor Boulevard
P.O. Box 152092
Irving, TX 75015-2092
214 718-6333

Kent B. Foster
President

December 19, 1989

The Honorable Daniel K. Inouye
Chairman, Subcommittee on Communications
Committee on Commerce, Science & Transportation
United States Senate
227 Hart Senate Office Building
Washington, D. C. 20510

Dear Chairman Inouye:

The Communications Subcomittee's hearings on cable television November 16 and 17, 1989, provided a useful forum for exchanging views on the relative merits of competition and regulation in video services programming and transmission. While we in the telephone industry appreciated the opportunity for GTE and the U.S. Telephone Association to testify, we also profited from simply listening to the representatives of other industries.

One of the witnesses was Edward O. Fritts, President of the National Association of Broadcasters (NAB). In his written testimony, Mr. Fritts recommended that telephone companies "not be permitted simply to purchase existing cable systems," but instead, "provide the second video wire to the home, wherever possible." He also stated that telephone companies should not be "owners of the content they carry."

Since my own prepared testimony deals with each of these points at pages 34-35 and 30-31 respectively, I would not be writing this letter if that were all Mr. Fritts said. I don't have a transcript in front of me, but if I heard his oral testimony correctly, Mr. Fritts declared that the telephone companies "lust after the cable model" of doing business.

In context, he seemed to be predicting that the telephone entry would simply redouble the problems now associated with cable TV's monopolistic position: "[U]nbridled discretion over carriage and the positioning of stations. . .the ability to act as gatekeeper to America's homes." (NAB written testimony, page 1)

Mr. Chairman, that simply is not the case. If telephone companies bring anything to the business of video programming and delivery, it is an alternative to the cable industry's closed model of operator-controls-all. The common carrier history of the telephone industry is one of open access. We build networks for use by the public. As I stated in my prepared testimony:

> [T]he switched architecture of the broadband telephone network offers an opportunity for a truly open market in which each subscriber has a vastly expanded range of choice, and anyone who creates a program can sell it to any subscriber. (page 15)
>
> Under the market structure I have described with competition from the cable company and with our transport available to anyone at tariffed rates, we will not be in a position to favor our own programming over that of any other provider. (page 31)

Thank you, Senator Inouye, for this opportunity to supplement the record of your November 17, 1989, hearings. GTE would be pleased to provide any additional information which may assist the Subcommittee's inquiry into these important matters.

Sincerely,

Kent Foster

Kent B. Foster
President - GTE Telephone Operations

KBF/cej

c: Edward O. Fritts, President - NAB
Albert Gore, Jr., U.S. Senator - Tennessee
Dean Swanson, Chairman - USTA Board of Directors
Members of Subcommittee on Communications

National Federation of Local Cable Programmers
National Headquarters
P.O. Box 27290
Washington, DC 20038-7290
202-829-7186

January 15, 1990

The Honorable Daniel Inouye, Chairman
Senate Communications Subcommittee
227 Hart Senate Office Building
Washington, DC 20510-6125

Dear Mr. Chairman:

In response to your invitation at the cable oversight hearings in November to comment on S. 1880, the National Federation of Local Cable Programmers has carefully considered the legislation introduced by Senator Danforth that would restore regulatory controls on the cable industry. We find that, while the bill offers much that we support, the needs of the public, educational and governmental access community are not adequately addressed by the proposed legislation.

As we outlined in our testimony before the Subcommittee, PEG access has achieved many successes in spite of problems caused for local access operations by the effects of the Cable Act. Our testimony documented the range and nature of the issues that confront access operations, even those that are recognized as among the most successful in the country. Our testimony also provided a set of legislative recommendations.

Senator Danforth's proposal addresses two of our concerns directly. S. 1880 redefines basic service to include PEG channels, which is a substantial advance. The bill would also restore rate regulation in many communities. Both these measures are welcome, and we fully support Senator Danforth's efforts in this regard.

However, the bill would not create the stable environment for PEG access that we feel is absolutely necessary if access is to live up to the potential that Congress envisioned for it. The bill would not ensure that access channels are provided on all cable systems; would not ensure that adequate operating funds can be secured for access operations, separate from the franchise fee; would not limit liability for access operations from suits based on access program content; and would not guarantee that access is available to all in the community, not just select groups. Our written testimony provides fuller explanation of these recommendations and provides additional suggestions. We believe that implementing these suggestions would minimize the problems now confronting cities such as Dayton, Ohio, which is facing great difficulty in meeting the well-documented cable needs of its residents, or Austin, Texas, where an outstanding access operation was almost dismantled by the local cable operator. We believe the modifications we are recommending would enable PEG access to fully mature as a ready conduit to the electronic marketplace of ideas for those who otherwise go unheard.

Cable's potential to make a unique contribution towards our nation's core communications policy goals of localism and diversity is directly related to the successful provision of public, educational and governmental access. These channels provide local programming that serves local needs, expresses local concerns, and reflects local diversity in ways that no other channels in the electronic media can match. The NFLCP hopes that the Subcommittee will recognize the specific needs of local cable programming and enact the changes necessary to bring national cable reality into line with national communications goals.

Thank you for this opportunity to express our concerns for the record regarding Senator Danforth's proposal. We look forward to continued work with you and the Subcommittee as you review cable policy.

Sincerely,

Sharon B. Ingraham
Chair

UCC UNITED CHURCH OF CHRIST
OFFICE OF COMMUNICATION
475 RIVERSIDE DRIVE, ROOM 852, NEW YORK, NY 10115-0109, (212) 870-2137

DR. BEVERLY J. CHAIN, Director

January 15, 1990

The Honorable Daniel Inouye, Chairman
Senate Communications Subcommittee
227 Hart Senate Office Building
Washington, DC 20510-6125

Dear Mr. Chairman:

The Office of Communication, United Church of Christ (OC/UCC), has been closely monitoring recent legislative proposals that address the flaws that have become apparent in the Cable Communications Policy Act of 1984. In light of the recent interest that has developed around Senator Danforth's S. 1880, and the reports that indicate that you may also be preparing legislation to modify the Cable Act, we would like to share with you the concerns that Senator Danforth's bill has raised for us as longtime advocates of the public interest in communications policy. These concerns arise both from what the bill covers as well as what it ignores.

S. 1880 addresses many traditional "public interest" concerns and does so reasonably well. The legislation's provisions to regulate rates, give cities more authority to deny franchise renewal, reimpose must-carry requirements, impose channel positioning rules, limit concentration of ownership, and regulate vertically integrated operators are welcome steps in the right direction. However, the must-carry provisions are flawed; the rate regulation proposal needs clarification; and public, educational and governmental ("PEG") access as well as leased access must be addressed.

Must-carry

While S. 1880's link between the compulsory license and must-carry makes sense and the protection for public TV is very welcome, the bill's must-carry scheme is flawed.

A) The bill does not advance the interests of the commercial stations that are most in need of must-carry protection, such as minority owned or ethnic language stations. Must-carry rules are sound public policy and advance traditional Congressional aims to the extent they protect smaller stations serving special needs. Network affiliates and VHF independents rarely need must-carry protection; it is in the cable operator's interest to carry these stations since these channels strengthen cable's value to consumers. (Indeed, despite the networks' declining audience share, cable subscribers continue to watch broadcast signals more than the 'cable-only' channels.) Start-up UHF's, especially those serving minority audiences, are most in need of protection, yet they are largely unprotected by this proposal since the operator has broad discretion to choose the broadcast signals to meet the requirements and the incentive to only program the most popular.

We are quite pleased that the bill will allow cities to require certain program services to meet community needs, and specifically mentions "programming that is in a particular foreign language or is of particular interest to a minority group comprising a significant portion of the population" in the community (at section 8(b)(3)). This is highly commendable, but it is unclear how this interacts with the must-carry provisions, and it does nothing for minority-owned stations or stations started once the franchise is signed.

B) The bill allows cable operators in some instances to choose which broadcasters they will carry. The proposed rules allow the cable operator to choose among broadcasters if there are more local stations than the bill dictates must be carried. Yet, in order for a must carry scheme to survive legal challenge, it must recognize that once the cable operator inserts itself into the broadcast scheme, it must do so fairly, i.e., it must carry all local broadcast signals. To allow cable operators to pick some signals and exclude others may give them extraordinary power over the viability of local broadcast stations, especially less powerful stations or those serving diverse needs or tastes.

C) The bill does not recognize the needs of the disabled or advancing broadcast technology. The must-carry rules only obligate the operator to carry the primary video and audio signals. Any material that is transmitted in the vertical blanking interval is carried at the discretion of the cable operator. This raises two problems: 1) Closed caption information and the experimental description service for the visually impaired are normally carried in this interval; where is the protection for these special needs? 2) The enhancements that may allow broadcasters to keep up with cable programmers, such as multichannel sound, additional information for advanced TV reception, or other such developments may be carried in this interval; leaving the carriage of such enhancements up to the cable operator may put too much power over the broadcaster's competitive ability in a competitor's hands.

PEG Access

Senator Danforth's proposal is largely silent on the issue of

PEG access, except to define these channels as part of basic cable service, which we applaud. However, PEG access, through which cable systems truly serve local needs and communities may realize the potential of broadband communications for community service, has been badly served under the Cable Act, which has not provided the fertile environment for access that Congress believed it had created in 1984.

Instead, PEG access has too often been buffeted by franchise modification requests, disputes with cities because of the Act's franchise fee language, problems securing funding in post-Act franchises or renewals, uncertainty about liability for program content, and the inability of many cities to effectively enforce the franchises they have or insure that the community's needs will be met at renewal. For cable to realize its potential as a communications medium that serves communities, and is thus integrated into national telecommunications policy designed to meet the full range of America's needs, OC/UCC urges you to add provisions that would meet the following goals:

- All cable systems should have at least one PEG access channel.
- Cities should be able to mandate that cable companies provide adequate support for the ongoing operations of access facilities (i.e., staff, outreach, training, promotion, administration, maintenance, etc.). Such funding should not be subtracted from the franchise fee, as it is now.
- Franchise fees should be earmarked for cable related purposes, including access support and franchise enforcement.
- Access centers should be clearly exempted from liability for access program content.

Leased Access

S. 1880 also does not mention the leased or commercial access provisions of the Cable Act, which by all accounts have been have been a failure. The fundamental problem with the Act's leased access scheme is that the operator sets a price and the potential lessee has to go to court with the burden to demonstrate that the price is unreasonable.

One alternative would be to: 1) require the operator to set a price at the fair market value of the channel based on the cost of providing the channel capacity; and 2) give the local franchise authority the right to use that standard to arbitrate any dispute between the cable operator and the prospective program supplier.

Another alternative would allow the operator and the program supplier to freely negotiate a rate. If they could not agree on terms, they would be bound to submit to "last offer" arbitration, where an independent arbitrator, chosen either by the franchise authority or a court of competent jurisdiction, would choose between the last offers of each.

Rate Regulation

S. 1880 would restore rate regulation to most municipalities, which we fully support as in the best interest of low income consumer or those on fixed incomes, who have seen cable prices rise without any alternative or competition to keep rates in line.

However, we are concerned that the bill mandates that any city that would gain the power to regulate rates is to establish a method for doing so in consultation with the operator of the affected cable system. Without some clarification as to the nature or extent of this consultation with the local operator (e.g., would the operator have the power to refuse the city's preferred method?) this clause could undermine the intent of this section.

Conclusion

Senator Danforth's proposal to restore some balance to the competing interests of cable operators, franchise authorities, potential competitors, broadcasters, and the general public, is a laudable effort. We would like to participate in the effort to craft a comprehensive policy that meets the full range of public needs and ensures that cable will join the ranks of communications systems that serve the "public interest, convenience and necessity." With the changes we are suggesting, we believe significant progress toward that goal can be made in the spirit of public service of all our people's communications needs.

Most sincerely,

Beverly Chain

Dr. Beverly J. Chain
Director

Andrew Blau
Assistant for
Communication Policy

Statement of
The United States Conference of Mayors
The National League of Cities and
The City of New York

Concerning

S. 1880,
The "Cable Television Consumer Protection Act of 1989"

January 15, 1990

Pursuant to the request of Senator Daniel K. Inouye, Chairman of the Senate Subcommittee on Communications, the United States Conference of Mayors, National League of Cities and the City of New York (collectively the "Cities") submit the following comments concerning S. 1880, "The Cable Television Protection Act of 1989."

S. 1880 represents a positive and much needed step toward resolving many of the problems which have arisen since enactment of the Cable Communications Policy Act of 1984 ("Cable Act"). The bill is designed to help protect consumers' interest in receiving quality, affordable cable television service. It seeks to achieve this important objective by enhancing competition to the cable industry and by reducing the barriers to franchising authorities' regulatory oversight of cable systems.

The Cities' specific proposals for addressing the various cable television issues are set forth in their paper entitled "Legislative Proposals to Alleviate Barriers to Effective Regulatory Oversight of Cable Television Systems and to Stimulate Competition in the Provision of Cable Television Services." As explained more fully in that paper, the Cities support many of the provisions in S. 1880. However, the Cities believe that these provisions may be strengthened in certain significant respects. Attached hereto is a "redlined" copy of S. 1880, reflecting the Cities' recommended revisions of that bill. What follows is a summary of those revisions by section.

1. "Regulation of Cable Rates;" Section 4: Congress intended in the Cable Act for cities to have regulatory authority over cable rates in franchise areas

not subject to "effective competition." However, the Federal Communications Commission ("FCC") circumvented congressional intent by defining "effective competition" as the presence of only three broadcast signals throughout a franchise area. As a result, cable operators in virtually every community have had the unrestrained ability to impose significant rate increases on consumers. Even the few cable operators subject to rate regulation under the FCC standard have been able to dilute the effectiveness of such regulation simply by increasing the rates for non-basic services and by removing popular programming from the basic tier -- thereby causing many subscribers to switch to a more expensive unregulated tier of service.

a. Scope of Regulation. The proposed standard in S. 1880, which defines "effective competition" as competition from another multichannel video programming distributor in a significant portion of a cable community, offers a realistic alternative to the FCC's "three broadcast signal" standard. However, Congress should strengthen the standard in S. 1880 by granting franchising authorities the right to regulate rates for all cable services in those areas not subject to "effective competition." The concept of "basic service" is increasingly becoming an anachronism as cable operators find new ways of marketing their services. By confining rate regulatory authority to basic service, Congress would simply provide cable operators with an easy means of circumventing the protection intended for consumers.

b. Standard for Regulation. Congress should clearly define in the Cable Act what constitutes "effective competition." Such a clear statutory definition of "effective competition" would eliminate concerns that the FCC might again undermine the intent of Congress and, thus, create the need for further congressional action, by enacting regulations broadly defining additional instances when a cable operator is "presumed" subject to "effective competition."

Two additional amendments should be made to S. 1880's "effective competition" standard. First, a franchise area should be considered subject to "effective competition" only if, at a minimum, there are two providers of comparable video programming and each: (1) offers cable service to at least 80 percent of the households in the franchise area; and (2) actually provides cable service to at least 30 percent of the households in the franchise area. Second, the definition should make it clear that "effective competition" must be provided by a non-affiliated cable system or other multichannel video programming distributor, and that such competition must come from a single distributor, rather than an aggregate of such distributors.

These amendments would ensure that competition exists throughout most of a franchise area. The standard proposed in S. 1880 raises concerns that: (1) some, but not all, of the cable operators and other multichannel video programming distributors in a franchise area may be subject to rate regulation; and (2) actual competition may not exist in a significant portion of a franchise area deemed subject to "effective competition."

c. Other Amendments. The Cities recommend the following additional amendments to the rate regulation provisions of S. 1880.

A franchising authority should have the sole responsibility for establishing a fair and efficient method of rate regulation. The requirement in S. 1880 that a franchising authority consult with the cable operator and the FCC places an unnecessary and potentially disruptive burden on a franchising authority's right to regulate rates.

Section 623(e), which restricts the right of franchising authorities to regulate rate increases not exceeding five percent per year, should be deleted. Cable operators could undermine the effectiveness of such a price cap in limiting rate increases by deleting programming from a service tier. This price cap also fails to take account of the unjustifiable rate increases that already have been imposed as a result of deregulation.

In addition to the December 29, 1990 report presently required by the Cable Act, the FCC should be required to prepare and submit to Congress another report four years thereafter. The additional study is necessary to determine the effect of the reregulation of cable rates on competition in the marketplace.

2. "Franchise Renewal; New Franchise Issuance;" Section 6: Franchising authorities have found that the Cable Act's renewal provisions make it extremely difficult to deny renewal of a cable operator's franchise. Most local cable systems enjoy not only a

monopoly, but a monopoly which Section 626 perpetuates. As a result, cable operators have little incentive to provide adequate service during the initial term of their franchise or to negotiate upgrades of that service; the Cities thus believe that Congress should repeal Section 626 and return to the status quo which existed prior to the Cable Act.

The renewal provisions in S. 1880, while not meeting the Cities' objective in eliminating Section 626, do represent an improvement over the current situation. The bill allows cities to consider competitive proposals for a franchise subject to renewal. It also increases the number of public interest factors that a franchising authority can consider as relevant to its renewal decision. It replaces the "preponderance of the evidence" standard of judicial review in Section 626 with an "arbitrary and capricious" standard, which is the one typically used for review of administrative decisions; in doing so, the bill offers greater protection to franchising authorities denying renewal requests that are not in the public interest. Finally, the bill deletes the "cure" provisions contained in Section 626(d), thereby ensuring that a cable operator cannot avoid the consequences of past breaches of its franchise agreement simply by correcting its behavior at some point in the distant future.

In several other respects, however, S. 1880 does not address the significant concerns which the Cities have with respect to the existing renewal provisions of the Cable Act.

First, under S. 1880, a franchising authority may not deny a renewal proposal which satisfies the standards in Section 626(c)(1) -- even if that renewal proposal is not comparable to proposals received from other cable operators. A franchising authority's right to solicit competitive bids can be rendered meaningless if franchising authorities cannot deny renewal and award the franchise to others who can better serve a community.

Second, the proposed revisions to Section 626(a)(2) in S. 1880 do not allow a franchising authority to consider the performance of an incumbent cable operator's predecessors in reviewing a renewal proposal. Cable systems are constantly being bought and sold by investors seeking a quick profit. Franchising authorities need to consider performances throughout the term of the initial franchise, and not simply the performance of the last cable operator to hold that franchise.

Third, the amendment to Section 626(b)(1)(A) in S. 1880 suggests that a franchising authority has no discretion in determining whether to solicit competitive bids. A franchising authority should not be forced to solicit competing bids if an incumbent's performance and renewal proposal satisfies the expectations of cable subscribers.

Fourth, franchising authorities should have the right to consider any factors "relevant" to the public interest in deciding whether to grant a renewal proposal or any other proposal. The "necessary to advance and protect" standard proposed in Section 626(c)(1)(E) of S. 1880 unnecessarily restricts the right of franchising authorities to consider other important public interest factors.

Fifth, the amendments to Section 626(c)(1) in S. 1880 do not make clear that franchising authorities have the right to consider, as relevant to their renewal decision, an incumbent's employment practices and the character of any party submitting a renewal proposal. Franchising authorities should not be prohibited from denying a franchise proposal submitted by a proposed cable operator of questionable character or from denying renewal to an incumbent whose employment practices are hostile to some segments of a community.

Finally, S. 1880 does not require agreement on the material terms of the franchise as a precondition to renewal. Absent such a requirement, the incumbent cable operator can easily circumvent the authority of municipalities to negotiate a renewal agreement which protects the public interest.

3. "Technical Standards;" Section 8: The FCC's antiquated, twenty-year old technical standards are meaningless for purposes of assessing the numerous complaints from cable subscribers about signal quality. The FCC has refused to update its standards, and has refused to allow franchising authorities to enact meaningful standards. Even if a cable operator complied with the existing FCC guidelines, the resulting signal quality could nevertheless be wholly unacceptable to a significant number of subscribers. Further, the present standards provide franchising authorities no meaningful basis to determine, as required by Section 626 of the

Cable Act, if a cable operator's signal quality has adequately served the needs of the community.

The Cities support the technical standards provision in S. 1880 since it would direct the FCC to adopt technical standards for signal quality which reflect contemporary technology, and periodically to adjust such standards to reflect advances in cable technology. Further, the provision would allow franchising authorities to adopt realistic standards which reflect individual community needs and conditions.

However, several amendments should be made in the proposed Section. First, Congress should add "time frames" to the technical standards provision so that cable operators have to comply with the new standards within a reasonable time period. Hence, the FCC should be required to prescribe and make effective contemporary technical standards within one year after enactment of S. 1880. Further, Congress should require cable operators to comply with the FCC standards, or standards established by a franchising authority pursuant to the Section, within one year after the FCC standards become effective.

Second, Congress should delete the provision in S. 1880 granting to any person aggrieved by the failure of a cable operator to comply with the technical standards the right to petition the FCC for a compliance order. Franchising authorities and the FCC will ensure that the standards are enforced. Third-party actions will only complicate and make more costly the regulation of cable systems.

4. "Limitations on Liability;" Section 7: The authority of cities to regulate cable is increasingly challenged in court on various statutory and constitutional grounds. These lawsuits are expensive for cities to litigate and expose municipalities to the possibility of extraordinary monetary judgments. As a result, the temptation is for cities to settle, rather than defend, their franchising authority in such suits.

The First Amendment immunity in S. 1880 provides needed protection to franchising authorities acting pursuant to the Cable Act or other applicable law. However, the immunity provision in S. 1880 would better achieve its intended objectives if several amendments were made.

First, a franchising authority should be immune from any claim challenging the authority's right to regulate a cable operator pursuant to the Cable Act and to applicable law, except for claims where an individual proves discrimination on the basis of race, color, sex, age, religion, national origin or handicap. If immunity is limited to First Amendment claims, cable operators may circumvent S. 1880 by simply bringing claims under the Fourteenth Amendment, Section 1983, or other arguably relevant federal and state law provisions.

Second, Congress should amend S. 1880 by deleting the provision in Section 628(a) which allows a cable operator to recover attorneys' fees. A city will be reluctant to defend its right to exercise its franchising authority if it must pay a cable operator's legal fees.

Finally, Congress should amend S. 1880 to clarify in Section 628(a) that immunity extends to decisions to renew or not to renew a franchise; to transfer or not to transfer a franchise; and to amend or not to amend a franchise.

5. "Regulation of Services, Facilities and Equipment;" Section 8: In view of the increasing vertical integration in the cable industry and the tendency of cable operators to carry affiliated programming, there is a significant concern that cable systems will drop programming of interest to a local cable community in favor of affiliated programming which is geared towards a national audience. The provision in S. 1880 allowing franchising authorities to require cable operators to provide broad categories of programming will ensure that cable subscribers have access to programming of importance to the local community.

Nevertheless, S. 1880 should be amended to expand the discretion of franchising authorities in requiring broad categories of programming.

First, instead of requiring in Section 624(b) that franchising authorities "shall" establish such programming requirements, the Section should state that franchising authorities "may" establish such requirements. A franchising authority should not be required to establish such standards if a cable operator is adequately serving local programming needs.

Second, instead of stating that required categories of programming must be "essential" to the operation of a cable system, Section 624(b) should provide that such requirements must "reasonably relate" to the operation of a cable system. The "essential" requirement is too restrictive and will lead to disagreements between cable operators and franchising authorities as to what is "essential."

Finally, although Section 624(b) states that the possible broad categories of programming are "not limited" to those specifically listed in the provision, Congress should clarify the nature of the programming which franchising authorities can require. In addition to the categories listed, Section 624(b) should state that franchising authorities may require a cable operator to provide news and public affairs programming; sports programming; and programming of particular interest to (i) the handicapped, (ii) children, and (iii) the elderly.

6. "Definitions;" Section 3(a): The definition of "basic cable service" should be deleted. The only purpose of the definition is to define the limits of rate regulation. However, for the reasons discussed above, the protection afforded consumers by rate regulation should not be limited to "basic cable service" alone.

7. "Definitions;" Section 3(c)(3): The term "cable community" should be amended to clarify that it includes the geographical area in which a cable operator is authorized by a franchising authority to provide cable service. The present definition only includes homes actually served in a franchise area.

The definition is used to define the area in which "effective competition" is measured. The amendment is needed to ensure that effective competition is present throughout a franchise area. Otherwise, competitors may meet the standard by providing cable service only to homes in sections of the franchise area with high population densities or in wealthier areas. If the standard applied to the entire area in which cable operators are authorized to provide service, then the cable operators would have an incentive to "effectively" compete throughout the franchise area in order to avoid rate regulation.

8. "Findings;" Section 2(2): The Cities recommend deleting the language which attributes to

"franchising requirements" the lack of local competition for video programming services. Local franchising requirements are not the reason most cable subscribers lack the opportunity to select between competing cable systems. The absence of competition at the local level is the result of: (1) the expense of constructing cable systems; (2) anticompetitive behavior by cable operators and their affiliated programmers against potential sources of competition; and (3) the infeasibility of overbuilds by potential competitors in many local areas.

9. "Requirement to Carry Local Broadcast Signals;" Section 5: The judicial elimination of the FCC's long standing "must-carry" rules reversed a twenty-year practice that formed the foundation of the relationship between the cable and broadcast industries. It threatens the continued availability to consumers of a broad array of local programming.

The Cities support the provisions in S. 1880 which would tie a cable operators right to enjoy the benefits of compulsory licensing to the carriage of local broadcast signals. Franchising authorities are prepared to exercise the role which S. 1880 would grant them in resolving disputes over the channel positioning of qualified broadcast stations if Congress establishes clearly articulated federal guidelines for exercising such power and if municipalities are granted immunity in any lawsuit challenging such authority.

10. Other Competitive Measures; Sections 9 and 10: The Cities support S. 1880's approach to resolving competitive problems in the cable industry. Competition in the industry will be promoted by provisions in the bill which: (1) limit the size of multiple system operators; and (2) prohibit programmers affiliated with cable operators from discriminating against nonaffiliated multichannel video programming distributors.

11. Additional Matters: S. 1880 addresses several issues of importance to franchising authorities, and the provisions in the bill would alleviate some of the concerns of franchising authorities with these issues. However, there are additional matters of concern to local franchising authorities which are not addressed in S. 1880, such as:

- consumer confusion resulting from the retiering of programming by cable operators;

- the uncertainty over the definition of franchise fees;

- the access of cable consumers to a "lifeline" tier of cable service containing vital programming;

- the judicial restraints on the ability of franchising authorities to enforce penalty provisions in franchise agreements;

- challenges by cable operators to a franchising authority's right to deny requests for franchises and to require that franchisees provide service throughout a franchise area;

- the barriers to the provision of cable television services by telephone companies within their local service areas;

- the ambiguity surrounding the jurisdiction of cities, states and the federal government in regulating cable television systems;

- the negative effects of trafficking in cable systems on the quality and price of cable service to consumers; and

- the unnecessary restrictions in the Cable Act on a franchising authority's right to deny modification requests not in the public interest.

These concerns, along with proposals to resolve them, are discussed in the paper accompanying this Statement.

National Cable Television Association

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January 17, 1990

Hon. Daniel K. Inouye
Chairman
Subcommittee on Communications
Committee on Commerce, Science, and Transportation
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

This letter is in response to your request for comments from the National Cable Television Association on S. 1880, the "Cable Television Consumer Protection Act."

NCTA represents more than 2,700 cable television systems serving 80 percent of the more than 50 million cable households in the United States; it also represents 56 cable programming networks engaged in creating and distributing a broad diversity of cable programming.

Later in this letter, each of the component parts of S. 1680 will be assessed; but some general observations may first be in order.

NCTA understands the concerns that have been expressed by some members of the Subcommittee about television, in general, and about cable television, in particular. We commend you for your leadership in addressing the complex issues that attend the Subcommittee's efforts to assure that television informs and entertains the public in a responsible fashion.

NCTA has supported the Subcommittee in these efforts. For example, as we stated before the Subcommittee at its October 25, 1989 hearing, NCTA supports Congressional enactment of a must carry statute to assure continued carriage on cable systems of qualified local broadcast stations. We support your proposal, Mr. Chairman, to let the Federal Communications Commission resolve through rulemaking the difficult issue of channel assignment.

As you know, NCTA also has no objection in principle to the proposal of Senator Danforth to include cable television within the time limitations that would be placed on advertising during children's television programming under the "Children's Television Act" (S. 1992), as reported by the Committee.

During the cable oversight hearings held by the Subcommittee November 16, 1989, NCTA and witnesses for some of its member companies indicated other cable-related issues that might be appropriate for a legislative solution; most notably, providing statutory disincentives to "traffic" in the ownership of cable television systems.

NCTA, as always, is ready to work with the Subcommittee on legislation that would provide the legal framework and incentives necessary to assure that the public receives the greatest benefits cable can provide. We believe that S. 1880, however, works against--not toward--achievement of that shared goal.

S. 1880 can be divided into several component parts: must carry, rate reregulation by city councils, franchise renewals, other city council regulatory issues, distributors' access to cable programming networks, and limitations on the corporate growth of cable companies. These issues will be examined in turn.

Must carry: NCTA's position on must carry has already been stated. We support Congressional enactment of a must carry statute that would both assure continued carriage on cable systems of qualified local broadcast stations and that would pass constitutional review by the courts. NCTA also supports your proposal to require the FCC to resolve through rulemaking the channel positioning problem.

However, we cannot support S. 1880's must carry provisions. S. 1880 would, in effect, condition use of the compulsory license granted cable under copyright law (17 U.S.C. 111) on compliance with requirements to carry certain broadcast stations on certain channels. The legislation would regulate the commercial relationships between broadcasters and cable in carrying these signals and between cable and its customers in providing these signals.

The Subcommittee held hearings on must carry on October 25, 1989, at which NCTA appeared and submitted extensive testimony, which need not be repeated here. Representatives of the broadcast industry also testified at those hearings, and it is instructive to note that S. 1880 goes far beyond the demands the broadcasters made at the hearing for a new must carry law. Among other things, it expands the number of channels to be set aside for carriage of local broadcast stations and it abandons the audience share test necessary to qualify for carriage. Both of these issues have been core components of a must carry compromise upon which the broadcast and cable industries have already reached general agreement.

The must carry provisions of S. 1880 go far beyond a compromise solution that NCTA could support. Indeed, the provisions go so far beyond a reasonable balance, and favor broadcasters so much to the direct detriment of cable networks, that NCTA suspects the courts would find S. 1880 violative of the First Amendment for the same reasons they have now twice invalidated FCC must carry rules.

Rate re-regulation: S. 1880 would authorize local city councils to regulate the rates for the basic cable service of virtually every cable system in the United States. This appears to be a response to some of the rate increases that occurred during the initial market adjustments that followed deregulation of those rates in December 1986. The proposal does not appear to admit consideration of the experience of the past year, which reflects cable's rate history after the adjustments were made.

The experience of the past year demonstrates that cable prices have stabilized. Cable rates now reflect both the value placed on cable programming by our customers and the pricing discipline imposed on us by our competitors.

As you may recall, a General Accounting Office study released last August found that the average cable customer's monthly bill increased by 14 percent from December 1986 to October 1988. The study found that the level of basic service most customers buy rose by about 26 percent during this same time period, from $11.70 to $14.77 per month. However, GAO also found that the number of program networks provided in this basic service package increased correspondingly, so that the price per channel of basic service remained constant during the period surveyed at approximately 45 cents per month.

The results of the GAO survey corroborate the increases in rates reported by the Bureau of Labor Statistics, which tracks price changes each month and which has provided ongoing information about the performance of cable rates in 1989. BLS, on December 19, 1989, issued its report on consumer price changes in November. Although the overall consumer price index rose by 0.2 percent, there was no change from October in the price index for cable television. This stability reflects the performance of cable rates throughout the first 11 months of 1989. During that period, cable rates rose only 2.1 percent, less than half the 4.5 percent increase in the overall CPI for the same period.

The GAO report and BLS statistics reflect a consistent picture: following deregulation, cable operators reconfigured programming packages (generally adding more services to the basic package) and adjusted the price to more accurately reflect the value (cable rates were held 72 points behind inflation during the years city councils were allowed to control them.) Those adjustments were largely completed by the end of 1988 and since then cable rates have remained stable, even lagging behind the overall rate of inflation in the economy.

The General Accounting Office is now engaged in an effort to update its study to include the period from October 1988 through December 1989.

NCTA acknowledges that individual cable systems in some communities have raised rates in excess of the national averages, in some cases by a significant amount. However, every serious examination of the performance of the cable industry nation-wide demonstrates that a reasonable equilibrium in pricing has been achieved.

At the same time, there is a general consensus, even among cable's harshest critics, that the quality, creativity, and diversity of programming provided by cable has improved dramatically since 1984. Indeed, a poll, commissioned by an agency of the National Association of Broadcasters, found that the public believes cable programming is superior to broadcast programming in every category except local news.

This improved quality in programming is a direct result of rate deregulation and renewal stability, both central features of the Cable Communications Policy Act of 1984. Freed from the caprice of city councils, cable operators have been able to price their services more in line with their value. And, with the assurance of renewal upon good performance, operators have a strengthened incentive to invest increased revenue in better product. For example, in 1984, cable operators spent about $300 million on basic cable programming. Last year, cable operators spent nearly $1 billion. This investment has led to the dramatic increase in both the availability and quality of cable program networks such as Nickelodeon, Discovery Channel, Black Entertainment Television, ESPN, and CNN.

Similarly, deregulation and renewal stability have enabled operators to increase substantially their investment in plant and equipment. Spending for this purpose has increased from about $200 million in 1984 to over $500 million in 1989. These investments also have benefited consumers by increasing the number of channels available and by improving the picture quality and reliability.

NCTA submits that a return to city council regulation of cable rates would be an overreaction to what was a transitional problem. Reregulation of cable rates by city councils would be a mistake. S. 1880's proposal to return regulatory authority to more than 9,000 different local city councils would choke off cable operators' investments in programming and plant and equipment.

Regulation of rates by city councils is not an economic decision, it is not even a regulatory decision; it is a political decision. No local politician has ever been reelected to office by reminding voters he authorized higher cable rates; however, many have campaigned on the platform that they kept cable rates down, even though rate increases may well have been justified.

There was much discussion, Mr. Chairman, during the Subcommittee's November cable oversight hearings about the competitive situation in the video distribution marketplace. Television broadcasters, satellite dish retailers, multi-channel, multipoint distribution service (MMDS), all presented their views of the situation and their visions of competition in the future. NCTA believes that it is essential that members of the Subcommittee are aware that each of these distribution technologies, as well as others like video cassette rentals and private satellite master antenna television services (SMATV), are all free from municipal oversight and are all unregulated. As competition between these technologies continues to grow, the idea of forcing cable systems, alone among these competitors, to submit to the control of more than 9000 different franchising authorities simply flies in the face of logic.

Freedom from local rate regulation has allowed cable to evolve into an effective competitor to the dominant means of television distribution: broadcasting. To return cable to the strictures of local rate regulation would diminish competition in video distribution, not bolster it. It should come as no surprise to the members of the Subcommittee, therefore, that cable's competitors are among the vocal supporters of rate regulation, for it is they, not consumers who would benefit if cable operators' incentives to invest in programming and plant and equipment are eliminated.

Renewal: The renewal provisions of S. 1880 are somewhat surprising for two reasons. First, no discernable problem exists with the renewal procedures and protections enacted by Congress in the Cable Act of 1984. There is no record before the Subcommittee of any defect in the existing statute. Second, the creation of renewal instability may well be the most anti-consumer provision of the entire legislation.

When Congress was considering the Cable Act, it wanted to ensure that cable systems provide the best service possible to consumers. Under the situation that existed at the time, cable operators had no assurance that their businesses would continue, regardless of how well they performed, and did not even have fundamental due process rights when seeking to renew or extend the term of their franchises.

Congress, quite correctly, recognized that this situation created economic incentives for cable operators to maximize return on investment during the term of the existing franchise, for they could not count upon renewal. In other words, the situation that existed then created the incentive to take as much out of the system as possible while putting as little back into it as possible.

With the Cable Communications Policy Act of 1984, Congress created a balance through which cable operators could expect renewal if they satisfied certain statutory criteria. Basically, these criteria assured renewal only in those situations where cable operators have lived up to franchise commitments, have provided good service, promise to continue to provide good service and make reasonable improvements. Franchising authorities can deny renewal to any cable operator who fails to meet these criteria. And, in order to ensure the decision on renewal is dispassionate, apolitical, and fair, cable operators are granted simple fundamental rights of due process.

This balance has provided stability for good cable operators, allowing them to plan for the long term, without unnecessary worry of confiscation of their assets upon expiration of the franchise. This stability has changed the pre-Act incentive to pocket as much revenue as possible into one that promotes reinvestment by cable operators in new plant and new programming which, in turn, provides major benefits to cable consumers.

At the same time, the renewal provisions of the Cable Act have worked no hardship upon franchising authorities. Since the enactment of the Cable Act, there has not been a single case in which a cable operator, denied renewal by a franchising authority, has gone to court and succeeded in overturning the city decision.

Despite any evidence of a problem between cities and cable systems in regard to renewal, S. 1880 seeks to skew the balance established in 1984 wholly in favor of franchising authorities. At the same time, it seeks to strip the cable operators of the due process protections guaranteed by the Cable Act. For example, if S. 1880 were law, cable operators involved in a renewal proceeding would no longer have the right to present evidence, would no longer have the right to compel the production of evidence from others, would no longer have the right to question witnesses. If S. 1880 were enacted, operators would need be given only "a fair opportunity for participation."

S. 1880 would allow each city council to establish its own standards for renewal, inviting return of the kind of unbridled political shenanigans that attended renewals before the Cable Act. S. 1880 would also effectively eliminate the ability of a cable operator who had been unfairly denied renewal to obtain relief from courts in all but the most egregious cases.

If enacted the renewal provisions of S. 1880 would remove the incentive for operators to reinvest revenues. Given the lack of any evidence of a problem in renewals and the virtual certainty that S. 1880 renewal provisions would hurt consumers, NCTA strongly opposes action in this area.

Other City Council Issues: S. 1880 would significantly expand city council authority in a number of key areas unrelated to rates and renewals. For example, the Cable Act protection against city council control of the content of cable programming would be repealed. S. 1880 would also reverse federal preemption of technical standards and, essentially, leave engineering decisions to local city bureaucrats.

As you know, Congress and the FCC have preempted local control of television content and have themselves imposed many requirements on both broadcast and cable, such as equal time for federal candidates and other election-related regulations. And, as mentioned earlier, NCTA has no objection in principle to the proposal of Senator Danforth to include cable in the commercial limitations of S. 1992, the "Children's Television Act." NCTA believes even-handed treatment between broadcasters and cable in these areas by the federal government is appropriate.

NCTA also believes the same should be true for technical standards for transmissions of broadcasters and cable operators. The FCC long ago preempted local control of the technical aspects of broadcast transmissions. In 1974, the FCC found it necessary to preempt the ability of cities to set standards for cable transmissions, although it allowed cities to enforce the standards set by the Commission. The reasons for this preemption are instructive. Prior to 1974, cities were free to establish their own technical standards. The FCC, which of course has substantial expertise in this area, found that the cities lacked comparable expertise. The standards set before 1974 were found to be unrealistic, unaffordable, and unnecessary. They were stifling the development of cable by balkanizing the industry. Preemption was the only solution to allowing cable to develop in an orderly fashion as national distribution medium.

The Cable Communications Policy Act of 1984 expressly reserved authority for the FCC to continue to preempt local control of cable transmissions. The FCC in 1985, after full participation of city organizations, the cable industry, and other interested parties, reaffirmed its 1974 preemption.

The National League of Cites, New York City, and others appealed the FCC's actions to the Court of Appeals for the D.C. Circuit. The court upheld the FCC's preemption, a decision that was affirmed by the U.S. Supreme Court. The Court of Appeals also remanded the rules to the Commission and suggested it develop its standards further. The FCC rules identify four classes of cable transmissions: retransmission of broadcast signals, retransmission of satellite-delivered signals, local origination by the operator, and two-way transmissions. Although preemption applies to all classes, the Commission has actually established quantitative standards only for the first class. The Commission currently has an on-going proceeding that may develop additional standards. NCTA has been working with the National League of Cities, the U.S. Conference of Mayors and others in an effort to reach a resolution of this dispute.

In assessing S. 1880's proposal to reverse federal preemption of local control over the content and engineering of cable transmissions, it is important to bear in mind that there are two main forms of television delivery in virtually every community in America: over-the-air broadcast and cable. The idea of giving local city councils control over broadcast content or transmissions is virtually unthinkable and a proposal to do so would have little, if any, support. NCTA believes cable should be treated no differently, and is firmly opposed to these two provisions of S. 1880.

S. 1880 contains another provision that would preclude monetary damages against cities for any First Amendment violation arising from regulation of cable communications, or from any decision to grant or not grant a franchise, or to otherwise regulate cable in a manner permitted by the Cable Act or other federal, state, or local law. This provision appears to respond to the fears of some cities that they may be sued for denying a franchise. A few years ago litigation was brought in federal court in California in which an applicant for a cable franchise sued the city for monetary damages under the Civil Rights Act because his application was denied. No court has ever ordered a city to pay such damages.

Nevertheless, NCTA is sympathetic to the problem of franchising authorities in their potential vulnerability for monetary damages based upon violations of civil rights. NCTA recognizes that the appeals courts and the Supreme Court are still in the process of defining the parameters of cable's First Amendment protections. Although NCTA believes that cities must remain subject to injunctive relief, it does not believe that franchising authorities should be liable for monetary damages or actions that are expressly authorized by the Cable Act and that are not now a clear violation of the First Amendment.

The provisions S. 1880, however, go too far. They would immunize a franchising authority from monetary damages even when it knowingly violates First Amendment protections. Further, when taken in conjunction with S. 1880's repeal of the Cable Act prohibition against municipal content control, this insulation from monetary damages is an invitation to direct and outrageous censorship by city councils. The civil rights of cable operators and programmers deserve no less protection than the civil rights of anyone in our society.

Access to cable networks by competing distribution technologies: S. 1880 would require cable networks with operator affiliation to make programming available to all financially qualified distributors, regardless of distribution technologies, at the same rates, terms, and conditions granted to cable operators.

This proposal is a permutation of a debate that has occupied the attention of the Subcommittee for a number of years now. NCTA has testified several times on this issue and our position need not here be belabored again. It is instructive, however, to review how the debate has evolved.

Initially, Congress received a deluge mail from worried satellite dish owners who feared that the advent of scrambling in 1986 would deprive them of programming. That fear diminished when dish owners found scrambled cable networks were available from a number of sources, in various combinations, and, as the Committee concluded in 1987, at prices comparable to -- and often less than -- those paid by cable subscribers for the same networks. Now, in 1990, dish sales are booming, programing subscriptions to dish owners are booming, and the former flood of complaints has trickled down to a small, dedicated, and vocal group of dish retailers who would prefer a lower wholesale price from programmers. The issue no longer is about consumer access to cable programing via satellite. The issue now is about the margin of profit dish retailers may pocket in selling cable programing to backyard dish owners.

Similarly, MMDS operators have joined the call for lower wholesale prices. Again the problem is not access to programing: all of the top 10 cable basic networks are sold to MMDS. Rather the problems in the MMDS industry seem largely attributable to undercapitalization, over-leveraged debt and mismanagement. They now want Congress to bail them out of these problems by lowering their wholesale prices in order to increase their margin of profit.

When the subcommittee held its hearings last summer on ownership in media, NCTA submitted a comprehensive study by Dr. Benjamin Klein of U.C.L.A. that demonstrated that cable operator investment in programing is largely responsible for the diversity of choices available to cable customers today. At the same time, this study indicated that cable operators with investments in programing have not carried those networks to the exclusion of non-affiliated networks, nor has vertical integration resulted in withholding product from competing distributors. Dr. Klein's work has been dismissed by some of our critics, but the analysis and findings of his study have not been refuted.

Fundamentally, S. 1880 would deprive cable networks with operator affiliation of control of distribution of their programming. The result would be diminished, not enhanced, competition.

Product differentiation is the key to successful competition in the distribution of video programming. Exclusivity over product promotes competition through diversity of choice, which is why programmers want to determine how and by whom their products are to be exhibited. Federal law has long recognized that by protecting exclusive rights to intellectual property, it enhances competition and provides for increased diversity of information and entertainment. Indeed, federal policy has recognized that disruption of these exclusive rights works against, not toward, competition.

Federal law does not mandate that a local movie theater or even a national chain of theaters is entitled to show any particular movie. It does not mandate that all television stations are entitled to network affiliation agreements, nor does it forbid a network-owned broadcast station from being programmed with the same network's "feed." For example, NBC may license its wholly-owned and operated broadcast station in Washington, D.C. (WRC-TV) as the only distributor of NBC programming in the Washington area, to the exclusion of other aspiring NBC affiliates. Cable operators who would like to be NBC affiliates are denied the opportunity altogether; NBC is a broadcast only programmer. Moreover, federal law does not permit a cable system to use its compulsory license to import network programming from an out of town NBC affiliate over the objection of a local affiliate of that network.

The federal government recently took steps to strengthen broadcasters' exclusive rights to programming. On January 1, 1990, a new FCC regulation went into effect that reinstated syndicated exclusivity for broadcasters; federal policy therefore does not permit cable to use is compulsory license to import programming from distant stations if a local station has the complete rights to a market for such programming. These rules were approved in December by the U.S. Court of Appeals for the D.C. Circuit.

At the same time the FCC reinstated syndicated exclusivity, it broadened the network non-duplication rules by expanding the situations where local broadcast network affiliates can prevent carriage of distant broadcast network affiliates.

Finally, just last year, Congress itself again recognized the need to protect program exclusivity in the Satellite Home Viewer Act of 1989. That law takes the programming covered by cable's compulsory license and extends a compulsory license to satellite carriers to make it available to home satellite dish owners.

Congress restricted that license, however, so that home dish owners may not receive network programming via satellite if they have access to a terrestrial broadcast affiliate of that network. The law also ordered the FCC to see if similar protection for non-network programming is feasible.

NCTA believes cable needs equal treatment under the law to compete effectively. Accordingly, NCTA opposes the provisions of S. 1880 that would single out cable networks and deprive them of the distribution prerogatives afforded their competitors.

Horizontal Concentration: S. 1880 would limit growth of cable operators to 15 percent of the national subscriber base. Currently only one cable company, TCI, would surpass that limit.

The Department of Justice uses the Herfindahl-Hirschman index to assess concentration. This index reflects the market share distribution among all firms in a given market, giving proportionately greater weight to market shares of the larger firms. Under this economic model, an index of 1,000 creates a threshold of concern that the potential for market share abuse by a single firm or a small number of firms within the industry may exist. Applying this index to the top twenty cable MSO's, the resulting value of 467 falls well below DOJ's threshold 1000.

The other generally accepted measure of concentration that could signal potential for abuse of market power is the top four firm ratio. Under this model, when the top four firms secure 50% of the market, the potential for abuse of market power exists. When applied to the cable industry, the top four firms garner only a 35% market share, again well below the level of concern.

Throughout the extensive hearings of the Subcommittee conducted last year in oversight of the cable industry, problems with horizontal concentration in the cable industry were alleged more through innuendo and implication than through presentation of facts. S. 1880's cap of subscribers at 15% of the national number is unsupported by any known economic theory or experience. Further, there is an absence of any demonstration of actual abuse. NCTA, therefore, opposes this cap.

Conclusion: NCTA remains committed to working with the Subcommittee to find genuine solutions to genuine problems. We remain committed to helping the Subcommittee enact a reasonable and constitutional must carry law. We remain willing to participate in a legislative process to amend or add to the Cable Act such provisions as are necessary and appropriate to promote the public interest and the competitive development of the television marketplace.

NCTA must conclude, however, that S. 1880 taken as a whole removes cable's greatest incentives to invest in innovation, creativity, technology, and service. For these reasons, we strongly oppose S. 1880.

Respectfully submitted,

James P. Mooney

James P. Mooney

cc: Hon. Ernest Hollings
Hon. John Danforth
Hon. Robert Packwood
Members of the Committee on Commerce, Science, and Transportation